S. Hrg. 98-253

UNIVERSAL TELEPHONE SERVICE PRESERVATION ACT OF 1983

JOINT HEARINGS

BEFORE THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

AND THE

COMMITTEE ON ENERGY AND COMMERCE
HOUSE OF REPRESENTATIVES

NINETY-EIGHTH CONGRESS

FIRST SESSION

ON

S. 1660

RELATING TO THE PRESERVATION OF UNIVERSAL TELEPHONE SERVICE

H.R. 3621

TO AMEND THE COMMUNICATIONS ACT OF 1934 TO ASSURE UNIVERSAL TELEPHONE SERVICE WITHIN THE UNITED STATES, AND FOR OTHER PURPOSES

JULY 28 AND 29, 1983

Serial No. 98-30

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UNIVERSAL TELEPHONE SERVICE PRESERVATION ACT OF 1983

THURSDAY, JULY 28, 1983

U.S. Congress, Senate Committee on Commerce, Science, and Transportation, and House Committee on Energy and Commerce,
Washington, D.C.

The committees met, pursuant to notice, at 9 a.m., in room SR-325, Russell Senate Office Building, Hon. Bob Packwood (chairman of the Senate Committee on Commerce, Science, and Transportation) presiding.

Staff members assigned to these hearings: Ward H. White, senior counsel; Christopher D. Corsen, staff counsel; and Thomas W. Cohen, minority staff counsel; Senate. Thomas M. Ryan; Timothy E. Nulty; and Mark MacCarthy, professional staff members; House.

OPENING STATEMENT BY CHAIRMAN PACKWOOD

Chairman Packwood.[1] The committee will come to order, please.

We are starting today the first of 2 days of joint hearings before both Chairman Dingell's and my committee, and it is very unusual that we hold joint hearings. We have done it only occasionally in the past. As I recall, the last time it was on the Marathon Oil situation, but this is the first time we have done it in the area of communications.

I hope that evidences to all of the witnesses and others covering these hearings the importance that Chairman Dingell and I attach to these hearings.

We will follow in the hearings today the normal process we follow in the Senate, and that is, apart from the opening statements, we will go in the order of first-come, first-served, in terms of asking questions. So I will start with an opening statement, and then call on Chairman Dingell and others who may have them, and then we will take the witnesses.

I will again ask the witnesses to limit their testimony to 5 minutes. Their entire statements will be in the record, and there will be ample time to expand on those statements in questions, because I think I can assure all of the witnesses that this will not be a passive panel as far as the Members of Congress are concerned.

My opening statement is simply this, that for the better part of 200 years, this country has had a policy of attempting to make transportation and communications available to everybody in this country. We did it in transportation with post roads and waterways and railroads and highways and air travel, and as technology advanced, we said there are certain areas of this country that cannot afford to pay their own way. But we have never in the past followed a policy of denial to those people of railroads or highways or anything else. If we followed that policy today, there would be parts of this country that would have no highways.

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[1] Senator Packwood presided over the hearing this day.

Even with deregulation of the airlines, we have subsidized air travel to make sure that at least some small towns which would otherwise not be able to afford air travel will get it.

We have also followed that policy in communications, whether it be the telegraph or the telephone. For years and years it has been the policy of this Congress, administered by the Federal Communications Commission [FCC], that we would use long-distance charges to help defray the cost of rural and residential rates, and that we would not require rural and residential users to pay the full cost of providing their own telephone service. We thought if we did that, there would be many areas of this country that could not afford telephone service, and many people within even some areas of the country that could afford it who could not afford telephone service. So that has been the policy of this country for a long, long time.

The hearings today on the two bills that we have before us, Chairman Dingell and Wirth's bill and mine, are really philosophical-type hearings. The differences between the two bills are relatively minor, and I am confident that those differences can be harmonized, but the real issue is philosophy: Should we continue to use long distance rates, that is, especially business use of long distance, to subsidize rural and residential rates?

The bills that we have introduced would say yes. There are many witnesses today that would say no, and that is a fair philosophical disagreement. But I would encourage the witnesses to address themselves to the philosophy, and to the extent that they agree with our philosophy but may not like one or another of the parts of the bill, they are welcome to comment on that, but I think the real issue is philosophical.

Last, I would say that just a few weeks ago we had a long debate in the Senate on cable legislation, S. 66. That bill has passed the Senate. It is now residing in the House. One of the issues that was raised by the phone companies, especially the Bell System companies, during that time was whether or not cable companies would be allowed to carry data on an unregulated basis..

The phone companies at the moment are regulated when they carry data and cable is not. The phone companies argued for a level playing field, but that is either here nor there in terms of this legislation right now. But one of the arguments they raised, and I can quote from almost all of the local Bell affiliates in many of the statements made by the supporters of an amendment on the floor of the Senate, where the phone companies were very, very solicitous of residential and rural rates, was that they indicated that if a cable bill passed the Senate as it came out of the Commerce Committee, it would do damage to those rural and residential rates.

Well, ladies and gentlemen, the total local revenue of the Bell operating companies that they now obtain from data transmission is about 1 percent of their total local revenues, give or take a quarter of a percent or half a percent—it varies from company to company. One percent of their total local revenues, and of all of the data transmitted, bearing in mind that only 1 percent of it, only 1 percent of their local revenues is data, of all the data transmitted, well over 90 percent of it is transmitted by Bell anyway.

So, had the phone companies won their amendment, the amount of revenue that would have been available to subsidize rural and residential rates was miniscule. Today we are faced with a change in policy by the Federal Communications Commission that is significant and substantial.

As far as the subsidy of residential and rural rates are concerned, I will be very interested particularly in the testimony from the Bell affiliates as to how they could express such extraordinary concern about rural and residential rates when we were considering the cable bill, when the amount of moneys involved would have made no difference in terms of the subsidy. I will also be interested in how they can be very concerned at that time about rural and residential rates, and as I read their testimony, seem to be less concerned on this occasion about a very, very major change that will affect rural and residential rates.

Chairman Dingell.

OPENING STATEMENT BY CHAIRMAN DINGELL

Chairman Dingell. Mr. Chairman, I thank you for your hospitality, and I want to express for myself and my colleagues from the House our thanks for your hospitality and for presiding over these joint hearings.

I would also like to say that we from the House are very proud to see the speedy, expeditious and capable fashion in which you are moving forward on the two bills that we and our colleagues, including my good friend, Timothy Wirth, the chairman of the subcommittee, have cosponsored today.

The bills are different in just one area, length. Your bill is shorter, which I suspect might indicate a better job of draftsmanship. However, Mr. Chairman, there is no difference in basic philosophy.

If there is any difference between you and I on this matter, it is simply that I do not think there is a subsidy from the long distance subscribers to the local service subscribers. I believe that a wise counting system simply assigns uses to encourage the best functioning of the system, and in my view, the best functioning of the system is achieved by universal service, by service available to the largest number of people, because that confers a startling and an important benefit upon the whole of the society.

It is with considerable distress that I have observed recent attempts to essentially dismantle universal service and confer different advantages on different persons. The consequences of this will significantly diminish universal service and significantly impair the rights and the opportunities of disadvantaged American citizens to this great communications system that we have built over the years.

I believe, as you do, Mr. Chairman, that this scenario is very bad. I believe our bills are philosophically identical. In minor particulars, they differ. I am satisfied that those minor differences can be fully corrected, and that we can move forward and deal with the question expeditiously.

Yesterday, the FCC began to recognize the political circumstances which have impelled the broad political and economic interest in the consequences of the AT&T divestiture and actions that the FCC has taken. Those actions, desirable though they might appear, are grossly inadequate in light of all of the circumstances. The time limits which remain for the Congress to act upon this matter make it obvious as to why you, Mr. Chairman, are moving forward with this legislation with my good friend, Tim Wirth, myself and our colleagues in the House, Mr. Wyden and Mr. Gore, who have joined in sponsorship of this bill.

We strongly believe the matter must be addressed. I would point out that the rarity of two committees of the different bodies meeting together to move legislation forward should indicate to all who know Senator Packwood, myself and Chairman Wirth that we are determined that this matter shall move quickly. We are determined that the goals S. 1660, cosponsored by yourself and many of your distinguished colleagues in the Senate, and of H.R. 3621, cosponsored by a number of us in the House, shall move rapidly toward enactment and signature by the President to address the severe problems and injustices with regard to telecommunications.

Mr. Chairman, I thank you.

Chairman Packwood. Mr. Chairman, thank you.

[The bills follow:]

II

98TH CONGRESS
1ST SESSION

S. 1660

Relating to the preservation of universal telephone service.

IN THE SENATE OF THE UNITED STATES

JULY 21 (legislative day, JULY 18), 1983

Mr. PACKWOOD (for himself, Mr. GOLDWATER, Mr. DANFORTH, Mrs. KASSEBAUM, Mr. PRESSLER, Mr. STEVENS, Mr. TRIBLE, Mr. ABDNOR, Mr. ANDREWS, Mr. BOSCHWITZ, Mr. CHAFEE, Mr. COCHRAN, Mr. COHEN, Mr. DENTON, Mr. DOLE, Mr. DOMENICI, Mr. DURENBERGER, Mr. GRASSLEY, Mr. HATCH, Mr. HATFIELD, Mr. HECHT, Mr. HEINZ, Mr. JEPSEN, Mr. LAXALT, Mr. MCCLURE, Mr. ROTH, Mr. SIMPSON, Mr. SPECTER, Mr. STAFFORD, Mr. WALLOP, and Mr. WARNER) introduced the following bill; which was read twice and referred to the Committee on Commerce, Science, and Transportation

---

A BILL

Relating to the preservation of universal telephone service.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Universal Telephone Service Preservation Act of 1983".

POLICY

SEC. 2. For the purpose of making available, so far as possible, to all the people of the United States, rapid, efficient, nationwide, and worldwide telecommunications services with adequate facilities at reasonable charges; for the purpose of providing universal basic telephone service at reasonable charges to rural and residential basic telephone customers; for the purpose of assuring that all providers of telecommunications services bear an equitable share of the costs of providing universal basic telephone service; for the purpose of encouraging continuing improvements in telecommunications technologies and service in all areas of the United States; and for the purpose of promoting safety of life and property through the use of telecommunications.

"EXCHANGE ACCESS

SEC. 3. Section 221 of the Communications Act of 1934 is amended by adding at the end thereof the following new subsection:

"(e) The Commission shall establish a system of exchange access charges in order to—

"(1) achieve equal treatment among all inter-LATA carriers and other customers using the services of exchange companies through direct or indirect connection;

"(2) assure that payments and assignments of costs relating to exchange access are carried out in a manner which is open to public examination and which ensures accountability to the public;

"(3) achieve flexibility in accommodating changes in market conditions and technology;

"(4) establish incentives for efficient investment decisions and technological choices; and

"(5) ensure that exchange carriers are compensated for their costs of providing exchange access.".

UNIVERSAL SERVICE COSTS; DEFINITIONS

SEC. 4. Section 201 of the Communications Act of 1934 is amended by adding at the end thereof the following new subsections:

"(c)(1) The joint board established pursuant to section 410(d) of this Act shall establish a universal service charge schedule to insure that basic telephone service will be available at reasonable rates throughout the United States. Such schedule shall take effect on January 1, 1986, or on the date of the termination of the current subscriber plant factor compensation arrangement, whichever first occurs. Such schedule shall designate universal service costs to be allocated to the Federal jurisdiction and provide for their collection by means of a universal service charge that is payable by any interLATA carrier or any provider of interLATA services or private system that connects directly or indirectly to any exchange carrier or any local exchange switched network used to provide basic telephone service.

"(2) Each exchange company that qualifies for payments shall be entitled to receive 90 per centum of its reasonably incurred universal service costs, which are directly related to the efficient and economic provision of such service.

"(3) For purposes of this title, universal service costs shall consist of an exchange company's costs for basic intraLATA telephone service to any points within a LATA which exceed 110 per centum of the average cost of providing comparable basic intraLATA telephone service throughout the United States.

"(d) Notwithstanding the provisions of subsection (c), any company which qualifies for payments under this section and whose costs for basic intraLATA telephone service to any points exceed 250 per centum of the average cost of providing comparable basic intraLATA telephone service throughout the United States shall be entitled to receive 100 per centum of its reasonably incurred universal service costs over 250 per centum of the national average.

"(e) For purposes of this section, the term—

"(1) 'basic telephone service' shall mean residential voice-grade communications provided to the general public on a universal basis over the public switched telephone network for use by natural persons to communicate with each other by voice;

"(2) 'basic intraLATA telephone service' shall mean that portion of basic telephone service provided within a local access and transport area (LATA) as that term was described in the plan of reorganization filed on December 16, 1982, in the United States District Court for the District of Columbia, in civil action No. 82-0192, and as approved by such court, including access to such service. Such term shall include service between independent telephone companies that are associated with Bell Operating Company LATA's and service within an independent telephone company service area which is the equivalent of a LATA; and

"(3) 'exchange company' shall mean a company that offers basic telephone service and other services within one or more service areas recognized by any State regulatory commission.

"(f) On and after the date of the enactment of this subsection, no interstate nontraffic sensitive costs shall be recovered from end users.".

JURISDICTION

SEC. 5. (a) Section 2(a) of the Communications Act of 1934 is amended by inserting immediately after "interstate" the first place where it occurs, a comma and "interLATA".

(b) Section 2(b)(1) of the Communications Act of 1934 is amended by deleting "intrastate communication service" and inserting in lieu thereof "exchange communications service".

(c) Sections 2(b) (2) and (3) of the Communications Act of 1934 are each amended by inserting immediately after "interstate" a comma and "interLATA".

(d) Section 221 of the Communications Act of 1934 is amended by adding at the end thereof the following new subsections:

"(f) In order to achieve consistency and uniformity of policy in regard to interstate and intrastate access charges, the Commission may assert jurisdiction over all nontraffic sensitive subscriber loop costs to the Federal jurisdiction.

"(g) The Commission may, by rule, delegate to a State commission some or all of the Commission's authority under this title with respect to (1) intrastate interLATA toll service, and (2) access charges for the interconnection of exchange communications service with interstate or intrastate interLATA toll service upon a finding that such delegation would promote the purposes of this Act.

"(h) The joint board established pursuant to section 410(d) of this Act shall establish guidelines consistent with the purposes of this Act which shall bind a State commission in its exercise of any authority delegated to it under this section.

"(i) For purposes of this section, the term—

"(1) 'nontraffic sensitive' shall have such meaning as shall be prescribed by the Universal Telephone Service Joint Board established pursuant to section 410(d) of the Communications Act of 1934; and

"(2) 'subscriber loop' means a path for communication between a subscriber's access point, excluding inside wire, and the exchange company's central switch, furnished expressly for the use of one subscriber, and in such a manner as the exchange company elects, either by wire, radio, fiber optics, or a combination thereof.".

UNIVERSAL TELEPHONE SERVICE JOINT BOARD

SEC. 6. (a) Section 410 of the Communications Act of 1934 is amended by adding the following new subsection at the end thereof:

"(d) The Commission shall establish a joint board which shall be known as the 'Universal Telephone Service Joint Board'. Such Board shall be composed of five commissioners of the Commission and of four commissioners nominated by the national organization of the State commissions (referred to in subsection (c)), and approved by the Commission. The chairman of the Commission, or another commissioner designated by the Commission, shall serve as chairman of such Board. The Commission shall refer any matter relating to section 201(c) and subsections (e), (f), and (g) of section 221 to the Board established by this subsection. Any decision of such Board arising out of or in connection with such matter so referred shall be adopted by the Commission as a final decision. For the purpose of acting on any such matter, such Board shall have all the jurisdiction and power of a board established pursuant to subsection (a) of this section.

"(e) Whoever, with the intent to deprive any exchange company of any revenue to which it is otherwise entitled in connection with access charges, transmits telecommunications in a manner so as to avoid accessing a local exchange for the purpose of avoiding the payment of such charges shall be fined not more than $100,000.".

(b)(1) Section 410(a) of the Communications Act of 1934 is amended by inserting "and subsection (d) of this section" after "409".

(2) Section 410(c) of such Act is amended by inserting "and subsection (d) of this section" after "409".

BASIC TELEPHONE LIFELINE SERVICE

SEC. 7. The Federal Communications Commission and each State regulatory authority shall take action to ensure that natural persons within the jurisdiction of such authority have access to basic telephone lifeline service which shall be the minimum capability necessary for basic telephone service.

DEFINITION

SEC. 8. As used in this Act, the term "telecommunications" means the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information, by means of electromagnetic impulses (including impulses of light), with or without benefit of any closed transmission medium, including all instrumentalities, facilities, apparatus, and services (including the collection, storage, forwarding, switching, and delivery of such information) essential to such transmission.

I

98TH CONGRESS
1ST SESSION

H. R. 3621

To amend the Communications Act of 1934 to assure universal telephone service within the United States, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

JULY 21, 1983

Mr. WIRTH (for himself, Mr. DINGELL, Mr. SWIFT, Mr. WYDEN, and Mr. GORE) introduced the following bill; which was referred to the Committee on Energy and Commerce

---

A BILL

To amend the Communications Act of 1934 to assure universal telephone service within the United States, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SHORT TITLE; TABLE OF CONTENTS

SECTION 1. (a) This Act may be cited as the "Universal Telephone Service Preservation Act of 1983".

(b) The table of contents for this Act is as follows:

TABLE OF CONTENTS

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Sec. 2. Statement of findings and purposes.
Sec. 3. Definitions.
Sec. 4. Access charges.
Sec. 5. Universal Service Fund.

Sec. 6. Universal Service Board.
Sec. 7. Depreciation.
Sec. 8. Interexchange tariffs.
Sec. 9. Provider of last resort.
Sec. 10. Lifeline telephone service.
Sec. 11. Prohibition against cross subsidy.
Sec. 12. Effective date.

STATEMENT OF FINDINGS AND PURPOSES

SEC. 2. (a) The Congress finds that—

(1) the fifty-year effort to bring affordable and universally available telephone service to the public has served the Nation well;

(2) universal telephone service has contributed to the Nation's economic, social, and political integration and development;

(3) the public benefits from universal telephone service because each telephone subscriber receives a more valuable service when virtually anyone else in the country can be called;

(4) significant rate increases will threaten universal service by forcing many Americans, especially the poor, the elderly, the handicapped, and those living in high-cost urban and rural areas, to discontinue their telephone service; and

(5) the national interest demands telephone service that continues to be universally available at affordable rates.

(b) The purposes of this Act are—

(1) to assure the availability to all the people of the United States, affordable, reliable, efficient communication services which are essential to full participation in the Nation's economic, political, and social life;

(2) to assure that the costs of maintaining such availability of services are equitably allocated among all users and providers of communication services who benefit from the availability of such services;

(3) to assure that the States have sufficient regulatory authority to maintain universally available and affordable telephone service; and

(4) to assure that the economy, general welfare, and national security of the United States will benefit from continuing improvements in telecommunications technology and the continued development of a competitive telecommunications industry.

DEFINITIONS

SEC. 3. Section 3 of the Communications Act of 1934 is amended by adding at the end thereof the following:

"(hh) 'Exchange access' means the provision of facilities, services, or other related functions by an exchange common carrier, to an interexchange carrier or other person providing interexchange service, for the origination or termination of interexchange communication, and includes the use of the subscriber loop.

"(ii) 'Direct interconnection' means the provision of exchange access through facilities specifically designated for such purpose by the exchange carrier involved.

"(jj) 'Indirect interconnection' means the obtaining of exchange access from an exchange carrier by any means other than direct connection.

"(kk) 'Exchange area' means the area within which telephone exchange service is provided, except that (i) an exchange area may not include an entire State, and (ii) an exchange area that includes any part or all of any standard metropolitan statistical area may not include any substantial part of any other standard metropolitan statistical area.

"(ll) 'Exchange carrier' and 'exchange common carrier' mean a carrier authorized by the State commission to provide telephone exchange service on a universal basis.

"(mm) 'Interexchange carrier' means a carrier that provides interexchange service.

"(nn) 'Interexchange service' means communication services provided among points in more than one exchange area.".

ACCESS CHARGES

SEC. 4. (a) Effective on the date of the enactment of this Act, the decision and orders of the Federal Communications Commission in C.C. docket numbered 78-72 (adopted December 22, 1982) shall cease to have effect. On and after such date of enactment and prior to the effective date of the system of access charges established under the amendment made by subsection (b), the applicable rules and procedures in effect immediately prior to the effective date of such decision and order shall apply.

(b) Section 221 of the Communications Act of 1934 is amended by adding at the end thereof the following new subsection:

"(e)(1) The Commission shall establish a system of charges to compensate exchange common carriers for exchange access, and to reform the system of settlements and jurisdictional separation of property and expenses in force on the date of the enactment of this subsection. The purposes of such system of charges shall be—

"(A) to compensate exchange common carriers for all costs associated with providing or making available exchange access;

"(B) to achieve equitable treatment of all interexchange carriers and other persons who benefit from the services and facilities of each exchange common carrier through direct or indirect interconnection for exchange access, and to prevent any contributions between exchange services or functions and interexchange services or functions of such carriers, except as provided in this section and section 225;

"(C) to ensure the continued universal availability of communications service provided by exchange common carriers at reasonable and affordable charges;

"(D) to assure that payments and assignments of costs relating to exchange access are carried out in a manner which ensures accountability and is open to public examination; and

"(E) to encourage efficient investment decisions and technological development.

"(2)(A) The system established under paragraph (1) shall provide that an exchange common carrier shall file to the Commission a tariff for exchange access for each of its exchange areas, including each service, facility, and any other supporting function provided by such carrier to interexchange carriers that directly interconnect with the facilities of such carrier. A carrier may file, or the Commission or State commission may require a carrier to file, a joint tariff for exchange access for all of its exchange areas within a single State until January 1, 1988, or such later date as the Commission may, by rule, provide. If more than one exchange common carrier serves an exchange area, such carriers shall submit a joint tariff for exchange access unless the Commission determines that submission of a joint tariff would not serve the purposes of this title, and shall divide revenues in a manner approved by the Commission. A State commission may authorize or require exchange common carriers within the State to divide revenues received from charges for exchange access.

"(B) Each tariff under subparagraph (A) shall specify separate charges for each type of exchange access on an element-by-element basis. The charges for each type of exchange access shall be justified by costs. No exchange common carrier shall charge any person for types or elements of exchange access which such person does not request and obtain. Any differences in charges to different persons shall be justified on the basis of differences in the costs of providing the services, facilities, or other factors of production involved.

"(C) Each tariff under subparagraph (A) shall consist of four charges to be recovered from interexchange carriers. Three of the charges shall encompass all costs associated with exchange access and one shall be the surcharge established and maintained under section 225. The charges of such tariff which encompass all costs associated with exchange access shall specifically identify separate charges for—

"(i) services, facilities, or other factors which are caused solely by the provision of exchange access;

"(ii) services, facilities, or other factors which are not identified under clause (i) but which are directly attributable to exchange access; and "(iii) the cost of other services, facilities, or other factors which are not identified under clauses (i) and (ii) but which are used jointly or in common to provide exchange services and exchange access, as ascertained and apportioned under this Act.

"(3)(A) Such system shall provide that an exchange common carrier shall submit to the Commission a tariff for exchange access available from such carrier for interexchange carriers or other persons who indirectly interconnect with the facilities of such exchange carrier.

"(B) Each tariff under subparagraph (A) shall include—

"(i) a charge for the direct costs of any services, facilities, or other factors required solely for the provision of such interconnection,

"(ii) a charge reflecting an appropriate portion of the cost of services, facilities, and other factors which are used jointly or in common to provide exchange service and exchange access, as ascertained and apportioned under this Act,

"(iii) a charge reflecting the availability of the facilities of the exchange carrier for exchange access as an alternative for indirectly interconnecting interexchange carriers and interexchange customers to the extent such facilities are not used for exchange access by such carriers and customers, and "(iv) the surcharge established under section 225.

"(4)(A) Such system shall provide that an exchange common carrier shall submit to the Commission a tariff under which any interexchange carrier or other person who, without direct or indirect connection to such carrier, and for commercial purposes, makes available facilities, services, or related functions for exchange access, comparable to those available from an exchange carrier for exchange access, shall pay a charge reflecting the availability of the exchange carrier's facilities for exchange access as an alternative for the facilities of such person.

"(B) Subparagraph (A) shall not apply with respect to any person who demonstrates to the Commission that comparable facilities, services, or related functions are not available from the exchange carrier involved.

"(5)(A) Provision of exchange access, and payment therefor, shall be solely in accordance with the applicable tariff, and all costs and payments associated with the provision of exchange access shall be recovered solely through such tariffs in accordance with this subsection.

"(B) The charges under paragraphs (2)(C)(iii), (3)(B), and (4)(B) shall be established so that the aggregate amount estimated to be collected under such charges are sufficient to recover the costs allocated to exchange access under this Act.

"(6)(A) Effective beginning 90 days after the effective date of this subsection, any person who owns or operates facilities to originate or terminate interexchange communication other than through direct interconnection shall notify the appropriate exchange carriers, the Commission, and the appropriate State commissions. Such notification shall be made by means of a summary form which the Commission shall prescribe by rule.

"(B) Any person who fails to comply with subparagraph (A) shall forfeit to the United States the sum of $50,000.

"(7)(A) The Commission, after consideration of recommendations of the Universal Service Board, shall establish practices and methods to ascertain and fully apportion the cost of services, facilities, and other factors used jointly or in common to provide exchange services and exchange access.

"(B) The Commission shall establish the forms for records, accounts, and memoranda to be kept by carriers providing exchange access in order to facilitate processing tariffs of such carriers. The authority to establish practices and methods under this subsection shall be exercised in a manner which reflects differences in the size and relevant characteristics of carriers.

"(8)(A) Nothing in this subsection shall be construed to require an exchange common carrier to allow joint ownership of its switching facilities or to require such carrier to allow location on its premises of equipment owned by other persons.

"(B) Nothing in this subsection shall require an exchange common carrier to bill customers of interexchange services, provided that no cost associated with such billing is included in the applicable tariff. Nothing in this subsection shall preclude an exchange common carrier from offering to bill customers of interexchange services, provided that the costs of such billing constitute an element in the applicable tariff.

"(C) The Commission may permit exchange common carriers which serve not more than fifty thousand customer access lines to use statistical cost data representative of such class of carriers to support tariffs for exchange access in lieu of individual cost studies.

"(9)(A) The Commission shall delegate to each State commission the authority established in paragraph (2), conditioned upon the compliance of the State commission with the requirements of this subsection, and with rules and procedures promulgated by the Commission thereunder.

"(B) Any interexchange carrier or customer which alleges a violation of paragraph (2)(B), (3), or (4) may petition the Commission for review of the relevant portions of any tariff filed with the State commission, whether or not such carrier or customer was a party to the tariff proceeding before the State commission involved. Any carrier or customer filing such a petition concurrently shall submit a copy of the petition to the State commission. The Commission may proceed to review the relevant portions of the tariff only if the State commission renders an adverse decision or fails to render a final decision with respect to such alleged violations before the end of the 60-day period following the submission of such petition to the Commission. The State commission, in connection with rendering a decision, may conduct such hearings, and accept or require the submission of such testimony and other information, as the State commission considers necessary or appropriate. The Commission shall have authority to affirm, remand, or modify the relevant portions of such tariff, taking into full account the views of, and record developed by, the State commission.

"(10)(A) The initial tariffs for exchange access shall take effect on July 1, 1985.

"(B) During the transitional period, which shall terminate when the system of access charges under this subsection goes into effect, common carriers shall continue to participate in the system of jurisdictional separations of carrier property and expenses in effect on July 1, 1983. The subscriber plant factors, and the rate element corresponding to separations and settlements in any agreement to provide exchange access, shall be in accordance with the most recent Commission decisions as of July 1, 1983, and thereafter shall not be subject to modification during the remainder of the transitional period except that the Commission shall adjust the subscriber plant factors and the rate element in any such agreement to account for any change in the Consumer Price Index for urban consumers. During such transitional period, persons obtaining exchange access directly from an exchange carrier for purposes of resale shall pay an amount equal to the amount paid carriers pursuant to any agreement to provide exchange access covered by this paragraph for similar services and related functions, except that, if the rate which a reseller pays for any service to be resold indirectly covers payments made for exchange access, then the reseller shall not be required to pay any additional amount for the exchange access for which payments already have been made. The Commission and the Universal Service Board shall permit the aggregation of costs and the division of revenues until the Universal Service Fund has been established and funded.

"(C) The initial tariffs specified in subparagraph (A) shall provide for adjustments during a 3-year period which ensure that all interexchange services and customers make an orderly transition from the level of reimbursements made as of the day before the date on which tariffs for exchange access first take effect to the level of reimbursement which will be paid under this section and section 225.".

UNIVERSAL SERVICE FUND

SEC. 5. Title II of the Communications Act of 1934 is amended by adding at the end thereof the following:

"UNIVERSAL SERVICE FUND

"SEC. 225. (a) To assure the continued availability of universal transmission services, including service in rural or remote areas, at reasonable and affordable charges, there is hereby established the Universal Service Fund. On an annual basis, the Universal Service Board shall determine uniform surcharges on the amounts collected by exchange common carriers under paragraphs (2) and (3) of section 221(e), such that the Fund is sufficient to make the payments under this section.

"(b)(1) An exchange common carrier is entitled to receive payments from the Universal Service Fund if it certifies to the Universal Service Board that its average costs for non-traffic sensitive facilities per customer access line is in excess of 115 per centum of the national average of such costs.

"(2) The amount of the payments under paragraph (1) in the case of any eligible exchange carrier shall be determined by the Universal Service Board under section 410. The percentage of the costs for which payments are made to any carrier under this section shall increase to the extent such average costs of such carrier increase above 115 per centum of such national average.

"(c) The Universal Service Fund also shall include a transitional account, from which any exchange common carrier shall be entitled to receive annual payments if needed to ensure that such carrier receives from charges for exchange access under section 221(e) and from the Fund for each calendar year an amount not less than the total revenues such carrier received for the equivalent of exchange access in 1982, reduced by (1) the value of terminal equipment and inside wiring which the Commission orders removed from the revenue requirements (multiplied by any applicable subscriber plant factor in effect on January 1, 1982); and (2) any cost of exchange access recovered in tariffs for exchange services pursuant to section 221(e).

"(d)(1) The Universal Service Board shall establish and oversee an exchange access board (consisting of representatives of exchange common carriers, interexchange carriers, and other customers directly obtaining exchange access) to administer the accounts of the Universal Service Fund. The exchange access board shall administer the accounts of the Universal Service Fund in a manner which expedites the disbursement of funds to exchange common carriers through the use of rules and procedures which eliminate burdens or delays in the certification or application process to the maximum extent practicable, and which permit disbursement decisions to be made on the basis of uniform, general, simplified standards of eligibility which are readily applied to the information and other data included in each application.

"(2) Payments from the accounts of the Universal Service Fund to individual exchange common carriers shall be subject to audit and adjustment by the Universal Service Board to ensure that—

"(A) any certification or application is valid and based upon proper allocation of costs in accordance with guidelines established by the Universal Service Board under section 410;

"(B) such payments are used to maintain reasonable rates or charges;

"(C) such payments do not remove incentives for the efficient provision of exchange service, except that any adjustment based upon the factor established in this subparagraph shall be effective only on a prospective basis; and

"(D) such payments do not unreasonably impede the entry and operation of competitive suppliers of exchange services.".

UNIVERSAL SERVICE BOARD

SEC. 6. Section 410 of the Communications Act of 1934 is amended by adding at the end thereof the following:

"(d)(1) Not later than 30 days after the effective date of this section, the Commission shall establish a Universal Service Board pursuant to subsection (c) for the purpose of—

"(A) ensuring equitable and efficient economic treatment of users of common carrier services and exchange services and carriers providing such services;

"(B) providing for an orderly transition to the system of charges for exchange access established under section 221(e); and

"(C) achieving cooperation between the Federal Government and the States in carrying out the purposes of this title.

"(2) In accordance with subsection (c), the Universal Service Board—

"(A) shall establish and maintain formulas consistent with the purposes of section 225 for defining and comparing national average costs and charges and uniform practices for determining the payments required by the Universal Service Fund, and shall oversee the distribution of funds from the Universal Service Fund by the exchange access board in accordance with section 225;

"(B) shall make such changes and modifications in the system of jurisdictional separation of carrier property and expenses in force on the effective date of this section as may be necessary or appropriate for the orderly transition to the system of charges for exchange access established under section 221(e); and

"(C) shall determine at regular intervals the relative assignment by exchange common carriers of the cost of factors of production which are used jointly or in common to provide exchange service and exchange access.

"(3) In making the determination specified in paragraph (2)(C), the Universal Service Board shall—

"(A) encourage reliance upon exchange common carriers as distributors of interexchange transmissions, and promote continued universal availability of transmission services provided by exchange common carriers at reasonable and affordable rates; and

"(B) take into account, consistent with section 221(e)(1)—

"(i) the cost of capacity or special characteristics required for exchange service and exchange access;

"(ii) investment and associated costs (including depreciation and maintenance) needed to provide plant availability to meet demand (including peak demand) for exchange service and exchange access; and "(iii) the use of exchange facilities for exchange service and exchange access.

"(4) The Universal Service Board may, in accordance with title 5, United States Code, appoint such staff as it considers necessary to carry out its functions under this Act.".

DEPRECIATION

SEC. 7. Section 220 of the Communications Act of 1934 is amended by redesignating subsection (b) as subsection (b)(1) and by inserting after subsection (b)(1) (as redesignated) the following new paragraph:

"(2)(A) State commissions shall have authority (i) to establish classifications for exchange facilities and the portion of facilities used jointly for exchange and interexchange services assigned to the States by the Universal Service Board under section 410, and (ii) to prescribe the methods by which exchange carriers shall recover investments in such facilities.

"(B) Such methods shall provide for recovery of investments in such classes of facilities in a manner which promotes the economic viability of the exchange carriers involved.".

INTEREXCHANGE TARIFFS

SEC. 8. The Communications Act of 1934 is amended by inserting after section 225 (as added by this Act) the following new section:

"INTEREXCHANGE TARIFFS

"SEC. 226. In the case of any interexchange service provided by any carrier under a tariff in effect July 1, 1983, which was filed jointly with another carrier or under any successor tariff in effect after such date (whether filed jointly or otherwise), the tariff applicable to such service provided by such carrier shall be based on the nationwide average of the cost of providing interexchange service.".

PROVIDER OF LAST RESORT

SEC. 9. The Communications Act of 1934 is amended by inserting after section 226 (as added by this Act) the following new section:

"STATE AUTHORITY TO REQUIRE BASIC ONE-LINE TELEPHONE

"SEC. 227. (a) A State commission may require any exchange common carrier to lease and maintain on request a single basic one-line telephone instrument, and associated inside wiring, to any subscriber (or group of subscribers at a single premise) within such State on the basis of a tariff that includes all costs of providing and maintaining such instrument and wiring.

"(b) For purposes of this section, the term 'basic one-line telephone instrument' means the type of basic two-way switched telephone instrument which the State commission determines to be generally available to the public and in use on the date of the enactment of this section, or which the Commission determines by rule to be generally recognized as essential for basic participation in nationwide telecommunications. In making any such determination, the Commission may not reduce the quality of the type of basic one-line telephone instrument available on the effective date of this section.".

LIFELINE TELEPHONE SERVICE

SEC. 10. Section 201 of the Communications Act is amended by adding at the end thereof the following new subsection:

"(c) Each State commission shall establish rules for the provision of lifeline telephone service by exchange carriers which consists of providing minimum telephone exchange service at a discounted rate for low-income residential customers.".

PROHIBITION OF CROSS SUBSIDY

SEC. 11. Section 201 of the Communications Act of 1934 (as amended by this Act) is amended by adding at the end thereof the following:

"(d)(1) No carrier or exchange carrier may use revenues from regulated communications services to defray any costs associated with its entry into or engaging in commercial activities the prices for which are not regulated by the Commission or any State commissions.

"(2) Neither the Commission nor any State commission may consider the revenues or profits derived from the offering of any unregulated products or services (other than printed directory advertisements) by any carrier or exchange carrier in determining the revenue requirements of any common carrier service of such carrier.".

EFFECTIVE DATE

SEC. 12. The amendments made by this Act shall take effect on the date of the enactment of this Act.

Chairman PACKWOOD. I will call on the other members now in the order in which they arrived. Congressman Bryant, I think, was the first one here.

Representative BRYANT. Mr. Chairman, I would prefer to defer to the chairman of my Subcommittee on Telecommunications, Congressman Wirth.

Chairman PACKWOOD. Congressman Wirth.

OPENING STATEMENT BY REPRESENTATIVE WIRTH

Representative WIRTH. I thank my colleague from Texas and my chairman, Mr. Dingell, and Mr. Packwood. I would only very briefly make three points. One, the fact that we are here in joint session, that there is so much attention now given to this issue—so many of our colleagues on the floor of the House are concerned about it—clearly indicates that now this is an issue whose time has come. The Congress must act, and I want to commend you, Senator Packwood, and my chairman, John Dingell, for very aggressive and speedy action, and we will move quickly.

The second point that I would like to make, which will come up in our hearings this morning with the FCC, was my disappointment in the major parts of what the FCC did yesterday, reflecting again the need for the U.S. Congress to move very aggressively.

The third point that I would make, in summary, focuses on the issue that we debated so much last year on the House side, and that is the need to assure both the universal service and efficiency in the network. I would again emphasize that these are often conflicting, and appear to some to be mutually exclusive goals. They do not have to be so.

We can encourage efficiency through competition and technological innovation, and at the same time assure universal service. Those are dual goals, and we cannot allow ourselves to be discouraged by the fact that sometimes they appear to be mutually exclusive.

I thank the gentleman from Texas for yielding. I greatly appreciate it.

Chairman PACKWOOD. Congressman Leland.

OPENING STATEMENT BY REPRESENTATIVE LELAND

Representative LELAND. Thank you, Mr. Chairman.

I want to commend you and Chairman Dingell for your leadership and your foresight with regard to this very important issue. There are few issues which will more directly affect American consumers or more directly impact their pocketbooks.

I am pleased we will have the opportunity this morning to discuss the future of the telephone industry and the concept of universal service. In discussing these issues, we must begin with the problems presented by skyrocketing local telephone rates.

Last month, Southwestern Bell, which serves my home State of Texas, filed a rate request with the Texas Public Utility Commission that calls for an increase of $1.7 billion in local rates. If approved, this rate request would increase the cost of one party residential service from $10.75 to $34.35. Many of my constituents cannot afford such an extraordinary rate increase, yet they can even less afford to be thrown off the telephone network.

In 1983, Mr. Chairman, telephone service is not a luxury. It is a necessity. We must approach discussion on these issues with that realization.

As we consider various legislative proposals concerning domestic telecommunications policy, there are a few principles which I believe are paramount. Any legislation in this area must include a provision establishing a universal lifeline service fund. In establishing such a fund, however, I hope we will give our highest priority to those consumers least able to afford an increase in their rates, the elderly, the poor, and the unemployed.

I am deeply concerned that the universal service fund which would be established by some of the legislative proposals we will be considering in the near future do not target assistance specifically to groups most in need of such assistance, but provide assistance generally to residents of certain prescribed areas regardless of ability to pay. Such an approach is not justified.

We also must insure that American consumers continue to receive service from an efficient, high quality, technologically advanced, competitive telecommunications industry. We must be very careful that any legislation we might develop does not stifle the burgeoning competition in this industry.

Finally, Mr. Chairman, as we are all aware, this is an extremely complex and rapidly developing area. Any legislation we might develop must be sufficiently flexible to meet new or unforeseen situations. It also should include provisions for a regular and automatic review by Congress.

I look forward to the testimony and comments of our distinguished assemblage of witnesses.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you.

Congressman Markey next.

OPENING STATEMENT BY REPRESENTATIVE MARKEY

Representative **Markey**. Thank you, Senator Packwood.

Today the House and Senate begin consideration of no less than 13 bills on the issue of universal telephone service. That is quite a legislative bounty at a time when only 4 months ago committee leaders in both Houses of Congress were predicting that we were unlikely to see common carrier legislation at all this year. Why the change?

I think that the change is a response to a perceived national crisis, the threat that millions of Americans, urban and rural, might lose one of modern life's most basic necessities, the telephone. Many in Congress, myself included, believe that such a prospect would result in the most serious of consequences, the creation of an information aristocracy and an information underclass in our society.

While I have been skeptical about the value of legislation to deal with this problem during this period of grave uncertainty, I think it is time for everyone involved in the process to recognize the overwhelming consensus of the members of both committees to have legislation this year. We may well be beyond asking, "Should there be a bill?" and now appear ready to ask instead, "What kind of bill should there be?"

On Tuesday, Mr. Luken and I introduced a bill which proposes one solution to this problem. The Consumer Communications Act of 1983, H.R. 3647, seeks to solve the impending difficulties which Members perceive in the telecommunications industry from a proconsumer, procompetitive viewpoint. I use both of these terms in the same breath because I remain convinced that competition will ultimately serve to build the best national telephone network, available to the greatest number of consumers at the lowest possible rates.

For those who still need proof that competition benefits their constituents, the consumers of this industry, I recommend the most basic evidence, the morning newspaper. There you will find ads selling telephones for under $10, or promoting long distance service at half the normal rate. Thus, I feel enthusiastic about dubbing the Markey-Luken bill as the proconsumer and procompetition approach.

What are the elements of the Consumer Communications Act? I believe that the act is best understood by grouping its provisions into five categories.

First, it softens the impact that legal and regulatory changes have on consumers without distorting the new competitive communications market. H.R. 3647 lowers the residential access charge to 50 cents a month in 1984, down from $2 a month under the FCC's plan. It proposes a 10-year as opposed to a 6-year phase-in of the charges. To make up the difference, it pegs business charges slightly higher. It also includes so-called provider of last resort safeguards for consumers and it eliminates over a 10-year period, the uneconomic trap of subsidizing local rates with heavy long distance add-on charges.

Second, it provides help to those who cannot afford basic telephone service in the new environment. The bill targets moneys for a special lifeline telephone service rate for low income Americans, recognizing that poverty is not a rural or urban problem. H.R. 3647 establishes a National Lifeline Telephone Service Fund to provide the resources needed to sustain such service. The fund is financed through a minimal surcharge on long distance usage and local network bypasses.

Third, it attempts to aid those in high cost areas without oversubsidizing the unneedy or promoting inefficiency in the national telephone network. Recognizing that some areas face particular problems, we have supported limited subsidies for high cost areas. H.R. 3647 adopts the joint board formula with its efficiency rewarding subsidy taper as a reasonable compromise between the differing approaches outlined thus far.

Fourth, it seeks to enhance the prospect for competition within the industry. To this end, we have suggested in this bill that jurisdiction over intrastate toll policy should be moved to the FCC in an effort to speed up the growth of competitive long distance service. Also, we have prohibited cross-subsidization of regulated and unregulated services so as to insure that all competitors are playing on a level playing field.

Finally, fifth, it hopes to improve the effectiveness of the reglatory process. The Consumer Communications Act provides for the funding of public participation at the FCC to improve the breadth of debate in that forum. It also insists that a comprehensive study even broader than the one the FCC ordered yesterday be conducted to examine the future of universal service and the basis for local rate increase requests. Reports on this study are to be made annually to the Congress and to the State commissioners.

In conclusion, Mr. Chairman, I urge all Members of both Houses to consider all the bills before us carefully, and not agree to any quick fix of one of our Nation's most important and successful industries. I especially urge my House colleagues to examine H.R. 3647 closely, and to join as a cosponsor of this bill in the weeks ahead.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you.

Senator Goldwater.

OPENING STATEMENT BY SENATOR GOLDWATER

Senator GOLDWATER. Thank you, Mr. Chairman.

First, it is a real pleasure for me to be at the same table with Chairman Wirth, who has done such an outstanding job on the other side of dealing with the confusion we have up here, and Chairman Dingell, who also has helped us tremendously.

I was just sitting here thinking that 63 years of my life have been spent in the area of communications, and I sit here wondering why I do not know more about it. I think the most important part of the world's progress, and I mean this, the most important progress we have made has been in communications. Ever since animals learned to talk to each other, ever since the smoke signal and the heliograph, we have had communications.

Mr. Chairman, we have come a long way since I first introduced comprehensive telecommunications legislation, S. 622, in March 1979, but in many respects, the policy established in that legislation is more appropriate for today's environment than it was in 1979. Despite the FCC's decision in computer II, despite the Senate passage of S. 898 in 1981 by a margin of 90 to 4, and despite the settlement between AT&T and the Justice Department of the antitrust suit, the communications industry and the American people are still faced with confusion.

Technology continues to advance without adequate policy guidance to insure that the benefits of those technologies are available to all Americans. All of us are struggling now with the question presented by the proposed AT&T consent decree and the future of our national communications system. Many of the details are not final, nor are the implications of this massive breakup.

Immediately after Congress reconvened in 1982, the Senate Commerce Committee held several days of hearings on the decree. We heard from the chairman of the board of AT&T, the Assistant Secretary for Communications and Information, the director of the Defense Communications Agency, and the Assistant Attorney General. Several of these witnesses were not enthusiastic about details of the proposed consent decree. However, all of them testified that they could make it work, and that the public interest would ultimately be served by its implementation.

I rather reluctantly agreed with their conclusion. I see now I was wrong. I fear that the breakup of AT&T is potentially the worst thing to happen to our national interest, particularly in the field of communications, that will ever happen or that has ever happened. I will be the first to admit that AT&T is not always the best company in terms of service, but it was far better than any other telephone company in the world.

When AT&T and the Justice Department decided to split up that company and settle the antitrust case, what has the result been? I can tell you from personal experience that local telephone service has slowly deteriorated. In three places where I spend most of my time, Arizona, California, and Washington, my telephone service has gotten shabby. I will say again that I believe that divestiture was and is a mistake. Bigness in itself is not badness, as far as I am concerned, and that applies to the telephone industry as well as to other industries.

As for S. 1660, the major goal of any legislation must be preservation of universal service. Universal service was a goal of S. 622. It was a cornerstone of the policy established in S. 898, and it is the principal thrust of S. 1660, which I happily cosponsored. S. 1660 provides a specific mechanism to insure that universal service will be preserved at reasonable rates.

Now, by imposing an access charge on all interexchange carriers that use local distribution systems, revenues would be available to insure that all Americans have access to reasonably priced basic telephone service. I must confess that I have reservations about this legislation. I am not sure how wholeheartedly I support any legislation, but I will support this bill, S. 1660, because I believe it is worth a try to see what can be done about insuring that all

Americans are able to have access to telephone service at affordable rates. That is essential.

If the FCC cannot do it, then the Congress is the only one left, and it can and must. It behooves us to try.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you.

Senator Pressler.

OPENING STATEMENT BY SENATOR PRESSLER

Senator PRESSLER. Thank you, Mr. Chairman.

In listening to the comments this morning, I am struck by the fact that we all are very doubtful about the benefits of the breakup of AT&T, but in no section of our country will its effects be felt more strongly than in rural and smalltown areas. Ranchers, farmers, those who live in small cities and towns will be hit the hardest. Indeed, one of our rural telephone cooperatives estimates that the increases in rates for farmers, ranchers, and people living in small cities and towns will be as much as two or three times more than the American citizen living in a big city.

Indeed, in some instances big city rates might actually benefit in the long run, where there are large numbers of people making more calls. But the fact of the matter is that when you get out into a sparsely populated area, where so much of our food is grown, and our national economy depends so much on agriculture, we are in a situation where telephone service will become so expensive as to be almost prohibitive.

In many small towns, such as my own hometown of Humboldt, S. Dak., which has 487 people, many of them senior citizens, telephone service will become a luxury unless something is done. So, as a cosponsor of this bill, I would say that the one segment of the American economy that will be hurt the worst unless we do something is the rural areas, farmers and ranchers.

People are just beginning to wake up to how serious this problem is. I was in Spearfish, S. Dak., just the other day, and met with a group of senior citizens. Over and over again they said that our main communication with the outside world is telephone, to call their children, and on limited social security benefits they have very few financial options.

In these hearings, I shall be speaking up very strongly for rural and smalltown interests.

Mr. Chairman, Congress has a responsibility to our people. Today's hearings is the first step in fulfilling that responsibility. Last December, I wrote the chairman of the Federal Communications Commission, explaining my objections to the directions being taken in FCC docket 78-72, the access charge proceeding. I do not believe that the residential end user can or should bear the burden of all phone costs.

In high-cost areas like my home State of rural South Dakota, such a shift in cost could drive many people off the telephone network. I am also skeptical of promises that lower long-distance rates will offset higher local phone bills. South Dakota has very few population centers which would attract long-distance competition and provide lower rates.

In my December letter to Chairman Fowler, I state what should be the underlying principle of any telephone legislation: A change in the existing subsidy mechanism can only be justified if it presents no danger to the continuing availability of universal telephone service at affordable rates. The FCC's access charge decision must be measured against this policy of universal telephone service.

We are here today to examine this decision and establish policies which take into account the changing marketplace environment for telecommunications service. If we accept the principle of a universally accessible telephone network, the members of these committees here should focus on several questions during these hearings.

Who should be subsidized? Who should pay for the subsidy, and how much? What enforcement policies are necessary to insure the subsidy?

I look forward to hearing from this very impressive group of witnesses. I have requested written testimony from the South Dakota Public Utilities Commission, the Bell operating company in South Dakota, and a number of small South Dakota telephone cooperatives and independent companies. I shall ask that these be made a part of the hearing record, because I think that my State of South Dakota is a unique example of the devastating impact that this action is going to have on telephone users in rural and smalltown areas, and I think that the example of what is happening in South Dakota will be repeated in rural areas all over our Nation.

I also commend the leadership of our committees and pledge my efforts to working for a comprehensive, substantive telephone bill which will benefit the American consumer.

Chairman Packwood. Congressman Wyden.

OPENING STATEMENT BY REPRESENTATIVE WYDEN

Representative Wyden. Thank you very much, Senator.

I want to start by congratulating you, Senator, for the leadership you have shown in this area. My idea of bliss is seeing more Oregonians in key committee chairmanships, and I want to congratulate you. I want to also thank my own chairmen, Chairman Dingell and Chairman Wirth, for the opportunity they have given me to participate in the development of the House legislation that we introduced last week.

Over the course of the next couple of days, the members of these committees are going to spend a good deal of time discussing universal service, access charges, local loops, bypassers, and the other seemingly unintelligible terms which make up the technojargon of the telephone industry, but as we do so, I hope we do not lose sight of the fact that what we are really talking about here has much less to do with jargon than it does with service.

Our mission is a simple one, and that is to insure that millions of Americans continue to have access to affordable phone service, and that we do not bring about a day when the old phrase, "Sorry, wrong number," becomes, "Sorry, no number." That is the threat. If we fail in our task, phone rates are surely going to escalate out of the reach of thousands, particularly rural Americans, senior citizens, and the poor.

I do not think Congress wants to allow the creation of a subclass of Americans who cannot afford a phone. The legislation we are considering today is a big step toward insuring that we are not going to let the line go dead on Americans of modest means. And let us make no mistake about it. If the lines do go dead in this country, we are all going to be poorer. It does not do much good to have a phone unless the person or business you want to call also has one.

With telephone service, as with so many other necessities, it just takes two to tango. This principle is something that has been too often ignored in the discussion of telephone service in this country. In the recent weeks since legislation was introduced, I have heard persons again and again express concern about whether or not one group should subsidize another.

I think this concern simply misses the point. I want to emphasize that these charges are not a subsidy. They are merely a cost of doing business. They are the affected groups' fair share of maintaining the phone system, without which they would not have much business. Because long-distance companies and others depend on the phone network, they must be expected to invest in its maintenance.

Now, it is true that some groups will be more severely impacted by phone-rate increases than others. Before I came to the Congress, I was director of the Gray Panthers for several years, and I have never seen the senior citizens as frightened as they are today about the prospect of huge hikes in their telephone service.

Millions of senior citizens are walking on an economic tightrope, balancing their food against their fuel, their fuel against their medical costs. If telephone rates go up abruptly, they could literally be pushed off that economic tightrope.

I do not think that Congress wants to stand by and watch while senior citizens are forced to pit one necessity against another. Many of the Nation's small businesses will also fare poorly if phone rates skyrocket. Not only will the higher rates be difficult for small businesses to afford, but if the phone system begins to shrink, so will the small business person's access to customers.

We already know the small businesses in this country are walking a thin line between success and failure, so obviously we have got big stakes in keeping phone rates down.

I have mentioned two groups, the elderly and small business, with which I am particularly concerned, but the biggest stake of all is the preservation of a high quality, affordable, universal phone system. Now, through State and Federal regulation and the inventiveness of the industry, we have bound this country together with satellites, fiber optics, microwave transmitters, basic black desk phones. I do not think we have come this far just to suddenly one day say that is enough, everybody on their own.

Frankly, Mr. Chairman, I do not want to see a society where some people in this country have access to micro-optics and the senior citizens will not be able to afford a telephone to call their doctor. So that is why I believe Congress ought to proceed with the corrective legislation, and congratulate my chairman, and particularly a fellow Oregonian, and I look forward to moving this legislation at the earliest possible opportunity.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you.

Congressman Swift.

OPENING STATEMENT BY REPRESENTATIVE SWIFT

Representative SWIFT. Thank you very much, Mr. Chairman.

I agree with so much of what has been said here this morning. I would like to maybe address a small confusion in this whole problem, namely, how come if competition is supposed to reduce our rates, why are the rates going up? What is wrong? Is competition not working? The question is, who is it working for?

In response to published comments by AT&T that the FCC's decision on access charges may not result in lower rates for long-distance, the FCC has asked AT&T to tell them by tomorrow why long-distance rates should not go down at least 15 percent. In its letter to the AT&T, the FCC has argued that its access-charge decision will transfer an increasing portion of AT&T's revenue requirements to end users—that is the current telephone industry jargon for customer, and that is all of us—and asked them why this should not result in lower long-distance rates.

These developments point up that consumers may not get all that they were promised by AT&T or by the FCC, and while I must certainly applaud the FCC's action to at least get something for the consumer, I am afraid that too few people realize how little good this will all do for the average residential and small business consumer. Even if the FCC is successful in getting rates to drop just a mere 15 percent, fewer than 1 in 25 residential consumers will benefit, and all but 13 percent of the business users will end up paying more, not less, than they do today.

Why? Because with a nationwide average of $8 a month for the access charge, a 15-percent drop in long-distance rates would mean that the average user would have to have an average monthly long-distance bill of more than $50 before they even begin to benefit. In fact, fewer than 4 percent of the residential users have a $25 long-distance bill in any given month.

Beyond that, in any given month, one person in six makes no long-distance calls at all, and two-thirds have long-distance bills below $4. What businesses will benefit? Nearly two-thirds of American businesses have monthly long-distance bills under $7, and 87 percent have bills lower than the $50 in any given month, that $50 break-even point at which maybe they begin to receive some reduction in their long-distance costs.

Today, just 25 major companies in the United States use long distance sufficiently to account for 15 percent of all the long-distance traffic themselves. Twenty-five individual businesses account for one-sixth of the interstate long-distance traffic. The FCC's access charge decision—and here is where we answer the question—is a massive shift of revenues from those 25 companies to small and medium-sized businesses and residential customers. It is those 25 large companies whose rates are going to go down substantially, and virtually everybody else is going to pick up the difference.

As the chairman said when he began, this is essentially a philosophical difference, and I am going to be intrigued to find what philosophy it is that indicates this result is a useful one, a fair one, an equitable one for Americans. Millions and millions of American people and businesses have made decisions about the telecommunications needs based on rules that have suddenly shifted.

Changing the rules is necessary as technology changes and as we make the transition from a regulated monopoly to a competitive industry. But as those rules are changed, it is not too much to ask that universal service be maintained, and that the average American gets some of the benefits that have been promised as well.

Thank you very much, Mr. Chairman.

Chairman PACKWOOD. Thank you, Congressman.

Senator Gorton.

OPENING STATEMENT BY SENATOR GORTON

Senator GORTON. Mr. Chairman, I am troubled, as I know everyone in this room is, by predictions of sharply higher local telephone rates beginning next year. Congress has worked for decades toward the goal of universal telephone service. It is unacceptable at this point simply, abruptly to change that goal and accept policies that force people who have telephones today to drop off the system. It is clear that the Congress must act to control the increases in rural and residential telephone rates.

The reasons behind rising local telephone rates are complex. The problem does not lend itself to easy solutions. At the same time that we want to assure universal affordable telephone service, we want to eliminate incentives to bypass the local exchange, to encourage the development of new technologies, and to make a transition to a more competitive marketplace. Some of these goals may not be compatible.

I expect these hearings to help to clarify the problems, and to help us find solutions. I would like to congratulate the Chairman and those other Members who have introduced legislation on this subject, who have taken the initiative to control local rates before they become a serious problem.

Chairman PACKWOOD. Thank you.

Senator Lautenberg.

OPENING STATEMENT BY SENATOR LAUTENBERG

Senator LAUTENBERG. Thank you, Mr. Chairman.

I am pleased to participate in this joint hearing. I want to make a brief statement, but I would like to preface that with an observation. I share the view of Senator Goldwater that the breakup of AT&T will cause great hardship for many of our citizens. I guess the only beneficiaries may ultimately be the investors, who were not doing badly anyway.

Unfortunately, we cannot guarantee cheap phone rates for all of our citizens any more than we guarantee cheap energy for all of our citizens. Costs are rising. We are all disturbed by projections of large increases in local telephone rates. Rate hikes in my State are projected to run as high as 150 percent. These are rate hikes that will drive many people to simply drop telephone service, unless we do something.

As this Nation proceeds in the information age, we cannot allow millions of Americans to be denied access to one of the most basic of our services, almost as vital as heat and light—telephone service.

The question is, how do we insure universal, affordable telephone service while at the same time promoting efficiency, competition, and technological progress? It is not an easy question to answer. We have before us various proposals to subsidize high cost access. I am concerned that they may impair the incentive to be efficient. They may assist some people who do not need help paying their phone bills, and ignore others who do.

I have proposed an alternative approach in S. 1677. It is called the Home Phone Act of 1983. It would target support directly to people who cannot otherwise afford basic access. I think that kind of an approach would cost less. It would preserve market forces, and would go a long way toward meeting our goal of insuring universal access to the telephone network.

I commend the leadership of the two committee chairmen for calling these hearings, and I am looking forward to exploring these issues in detail.

Thank you, Mr. Chairman.

Chairman **Packwood**. Folks, I wonder if I might ask this. We have got three Senators and three House Members left to make opening statements. Governor Orr, testifying on behalf of the National Governors Association, has to leave at about 10:15 to 10:20 or else change plans that he is very reluctant to change, so I would hope that we could finish our opening statements by 10 and get the Governor on at that time. If not, I think I will interrupt the opening statements and put you on, Governor.

Congressman Bates.

OPENING STATEMENT BY REPRESENTATIVE BATES

Representative **Bates**. In light of your comments, I will be very brief. I have introduced three bills that I think are of the pro-competition, pro-consumer model, and I hope that those guidelines will be kept in mind as we go through this very complex matter.

I am a little concerned that there is an overreaction to the term "universal service" without defining what that service is, because in most of the phone company rate hikes that have been proposed, they do maintain universal service at a very low rate for certain customers.

So I think we need to address the overall structure, and if we are going to break up the world's largest monopoly, I think we have got to do it in a way that we go beyond maintaining these built-in subsidies, and I see a real problem between the rural areas, which need these subsidies, but only in the transition, until the competitive model gets in place, because if we lock in these large subsidies, I think California phone users would rather take their chances with lower long-distance rates and be subsidizing farmers or ranchers or ski resorts in remote areas, and I think that the phone companies want us to prohibit the bypass.

It seems to me the bypass offers the opportunity for getting the competition and getting the rates eventually down, and we should only do that or regulate the bypass in a way that encourages the different options of technology without building in too large a subsidy that we find 3 or 4 years from now we are locked into a system that is inefficient, ineffective, and very costly, and we have all the disadvantages of bigness instead of the decentralization and competition that we can get now.

I would like to get things back to a true cost, competitive model, and try and protect the consumers, because I think Mr. Swift's point that the 25 major companies that are really getting the benefit at this point of the changes should be focused on, and I hope it will by this panel.

Thank you.

Chairman **Packwood**. Thank you.

Congressman Whittaker.

OPENING STATEMENT BY REPRESENTATIVE WHITTAKER

Representative **Whittaker**. Thank you, Mr. Chairman.

I, too, will be brief. Let me just state that we have incurred in this country a long-term practice of subsidization of local rates by the use of revenue from long-distance rates. There are some that would propose that that should continue to be, but if it does, it will amount in 1984 to virtually everyone paying something like 17 cents a minute in subsidy every time they make a long-distance call.

I frankly think that in the long term, it probably makes more sense to reduce or to eliminate the subsidies if such action does not mean that local rates will increase so substantially that universal availability of local telephone service is threatened. The reduction or elimination of subsidies will result in economic efficiency and will promote technological innovation.

A few of my colleagues in the House and Senate Commerce Committee appear to have concluded already that a reduction or elimination of the subsidies will threaten universal telephone service. Thus they have proposed legislation that would basically continue the subsidization. Again, the promise of these legislative proposals is that continuation of these massive subsidies is necessary to preserve universal telephone service. Personally, I am not quite so sure that that is true. I do not know of any substantial evidence that indicates that continued massive subsidization is essential to the preservation of universal telephone service.

My own preference is that we phase out these subsidies over an extended period of time. If we do this over a long enough period of time, we can minimize the rate impact on our local telephone customers, and we can move to an economically efficient and competitive telecommunication environment.

I have introduced legislation this week that takes this approach of slowly phasing out the subsidies, and I am not alone. My bill has been cosponsored by two other members of the House Commerce Committee, Mr. Tauke and Mr. Nielson. Let me state perfectly clearly here, because I do not want any consfusion, universal telephone service must be preserved. We should continue to study telephone pricing to insure that universal telephone service is maintained.

If, after further analysis, it appears that universal service is threatened, we should pass whatever legislation is necessary. In this regard, I was pleased to learn that the FCC began an investigation yesterday to determine the impact of its regulatory decisions and the impending divestiture of AT&T's local telephone companies on local telephone rate. Evidence compiled from this investigation will be helpful to our committee in evaluating whether legislation to continue massive subsidies is needed, but at the present time, I think my bill just may do the job of minimizing local rate increases while simultaneously promoting efficiency and a competitive telecommunications environment.

Thank you.

Chairman PACKWOOD. Thank you.

Congressman Lent.

OPENING STATEMENT BY REPRESENTATIVE LENT

Representative LENT. Thank you, Mr. Chairman.

The legislation we are about to consider addresses a highly complex matter that requires close examination of a number of related problems. The bills would in effect abolish an access charge plan developed by the Federal Communications Commission over a 5-year period, and involving the input of scores of interested parties representing every point of view.

In place of that plan, the legislation would establish a total new charging methodology which was devised only recently. I am deeply concerned about the implications for the telephone customers of New York. I am also concerned about the impact of these proposals on the telephone companies serving these customers. Access charges will represent a significant segment of their revenues in 1984, and to the extent that the bills do not measure up to the assertions of their supporters, the ability of the telephone companies to serve the State will be jeopardized.

So, I urge that we consider and deliberate on these complex issues, and not rush into a solution which in the long run could damage an industry which is so important to the country. Any solution should be in the interest of consumers, the telecommunications industry, and perhaps most important, the public interest, what is best for the country over the long run.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you.

Senator Stevens.

OPENING STATEMENT BY SENATOR STEVENS

Senator STEVENS. Mr. Chairman, I am mindful that as a former Hoosier, my good friend, the Governor of Indiana, is waiting. Let me commend to you and the committee the bill that we introduced, S. 1382, which has been cosponsored by Senator Pressler, Senator Hollings, and Senator Exon. I do believe Senator Pressler has spoken at length on that.

I also want to express my regrets that I will not be here to introduce the former member of the State legislature and our commissioner of administration, my good friend also, Lisa Rudd, from Alaska. She will speak on the Alaska point of view. I think she will make clear that Alaska, of all States, is totally dependent upon the outcome of the hearing that you and Chairman Dingell are conducting, and we want to work with you every step of the way.

It is essential that the concept of universal service be defined by the Congress, and that we take action to proceed and make clear that this is a matter Congress is going to retain jurisdiction over. Your bill I have also cosponsored. I think there is a meeting of the minds here that can be reached, and I hope can be reached quickly enough to prevent real serious harm to those of us who represent the vast rural areas of our country. Thank you very much.

Chairman PACKWOOD. Thank you.

Senator Riegle.

OPENING STATEMENT BY SENATOR RIEGLE

Senator RIEGLE. Thank you, Mr. Chairman.

I will be very brief. I want to associate myself with the remarks of Senator Lautenberg, which I think are very important for us to consider. We do have a problem here, however, I think we can solve it. I think we must keep telephone rates within the reach of all citizens. I think we have got to assure that the burden of rising phone rates does not fall on the little people of this country. And I think we have the capacity to prevent that from happening.

Finally, I do not think we should have subsidy mechanism that penalizes certain States to the advantage of other States. I think it is essential to find a system that is balanced between the States as well as meeting the problem of individual citizens. I think we can find that answer if we work together.

Chairman PACKWOOD. Senator Ford.

OPENING STATEMENT BY SENATOR FORD

Senator FORD. Thank you, Mr. Chairman.

I will make an observation more than I will make a statement. I serve on the Energy and Natural Resources Committee, and in 31 days, over 2½ months, we have been trying to mark up the deregulation of the natural gas bill. We finally sent one to the floor yesterday without recommendation.

I believe, Mr. Chairman, the emotion natural gas prices cause around this country will pale in comparison to the problems that we are beginning to face here today.

Chairman PACKWOOD. Thank you.

We will conclude with Senator Danforth.

OPENING STATEMENT BY SENATOR DANFORTH

Senator DANFORTH. Thank you very much, Mr. Chairman.

I think Senator Ford has said it very well. I think what we are facing here is the natural gas issues revisited. In my State of Missouri, Southwestern Bell, which serves our State, has requested a record $254,800 million rate increase. I am told by the Missouri Public Service Commission that this means a basic residential rate increase of 99 percent to 164 percent, depending on the sparseness of population throughout the State.

In addition to that increase, the Federal Communications Commission's announcement with respect to long-distance access charges would mean, I am told, a minimum of $2 up to $23 a month charge paid by telephone users in Missouri even if they did not use their telephone.

Now, Mr. Chairman, I do not understand how increases of this sort could conceivably be in the interests of the consumer of telecommunications of our country, and for that reason I am pleased to cosponsor your legislation.

Chairman **Packwood**. Thank you very much.

Governor, you have been very, very patient.

We will now start with our witnesses, the first being Gov. Robert D. Orr, of Indiana, speaking today on behalf of the National Governors Association. Governor Orr is the chairman of the Committee on Transportation, Commerce, and Technology of the National Governors Association. It is good to have you with us.

STATEMENT OF HON. ROBERT D. ORR, GOVERNOR, STATE OF INDIANA, AND CHAIRMAN, COMMITTEE ON TRANSPORTATION, COMMERCE, AND TECHNOLOGY, NATIONAL GOVERNORS ASSOCIATION

Governor **Orr**. Chairman Packwood, Chairman Dingell seems to have vacated his seat, but Members of the Senate and House of Representatives, I thank you very much.

I thank you for the opportunity to appear this morning, and as you indicate, I do represent both the State of Indiana as well as the National Governors Association. I have what I hope is a brief enough statement to fit within your time, and I will be happy to answer your questions.

On behalf of the State of Indiana and my fellow Governors throughout the Nation, I deeply appreciate the opportunity to present these comments to the honorable members of this historic joint hearing on universal telephone service legislation.

The issue of assuring quality affordable telephone service to all American citizens demands the highest attention of the Congress. I strongly endorse your recognition of the immediacy and the magnitude of the problem. I also applaud the expedited and unified approach by which you are seeking to fashion an adequate statutory solution. Past inaction by Congress has allowed tremendous confusion and uncertainty that exists to continue until now. Because of past actions of the Federal Government through its judicial and administrative bodies, there is a potential that many segments of my constituency in Indiana will be without telephone service. Let me repeat: Totally without telephone service, because of its cost.

Today my concern is for the elderly, the indigent, small businessman, and farmer, and mostly rural phone users who face the prospect of bearing the so-called full cost of local service. Many, if not most, cannot afford that full cost. My Hoosier constituents are not yet as aware of the telephone issue as they are of the natural gas issue. But I can assure you that as soon as the first phone bill comes in next winter, they will be camping on my doorstep.

I am here to let you know and to let them know that the problem has to be dealt with here, not back in Indiana, not in the States, but here in Washington. My hands are tied. Congress must act, and act quickly, to regain control of this situation and prevent these serious problems from occurring.

Parenthetically, let me add that natural gas is still as important an issue as it was when I testified before the Senate Energy and Natural Resources Committee last spring, and I thank Senator Ford for bringing the subject up. Congress is apparently not going to act on that serious matter. In my opinion, this is an inexcusable dereliction of duty. We are now 3 months closer to the date when natural gas bills go through the ceiling again. Once frigid weather hits us next winter, and consumers begin howling once more, and with ample justification, they will be howling very loud indeed.

You and your colleagues in the other parts of the Congress need to be worrying that escalating natural gas bills and sudden large increases in phone bills will be arriving in people's mailboxes simultaneously. Some may very likely camp on your doorsteps as well.

Congress has loosened the regulatory bonds which kept the free market from working its will in the communications industry, and in turn this has permitted the introduction of products and services which have truly advanced the science and business of electronic communication.

As a Republican Governor, I would be hypocritical to the philosophy of my party to decrie the good effects of free market economics. The freer the market, usually the more efficient the allocation of goods and services. In the case of telephone service, as with nearly every segment of our economy, national policy must dictate some of the boundaries of the free market.

I am here today to suggest that the national good requires boundaries to free enterprise in this case, and to support in principle an acceptable middle ground in this question of deregulation. Let us have fair competition. Let us not have a cost based pricing system which destroys the concept of universal service.

This Nation has the widest proliferation and saturation of telephone service in the world. This provides us a communications network that is second to none. It is of national significance beyond the specific benefits enjoyed by the individual user. We must not create barriers which reduce access to this network, for that reduces the value of the network to everyone.

In short, if necessary, we must be willing to provide basic telephone service at a price below its actual cost. I am not, however, prepared to support any specific proposal for a national universal service fund created by charging long distance charges to help defray the cost of local services.

I accept the fact that Indiana residents will gain by having a policy that insures universal access in all States. I am concerned that according to the information provided to me, the national universal service fund provided by some of the proposals would result in Indiana telephone users contributing no less than $12 million to other States. We would receive approximately $1 in return for every $4 that we contribute.

I must take a strong position that in addition to providing universal service availability, Federal legislation on this issue must also provide clear statutory responsibility for some State control of intrastate telephone rates. By doing so, you can provide a means for States to assist in providing additional relief if required through the provision of local services and thereby perhaps minimize the degree of subsidy required at the national level.

Expanding that same analysis to five Midwestern States—Ohio, Michigan, Wisconsin, Illinois, and Indiana—the net outflow of revenue to help support telephone services in other parts of the country would be in excess of $80 million for those five States.

I have serious reservations about that level of interstate transfers of revenue. However, I can accept the fact that some method of charging long distance providers to help defray the cost of local services would be appropriate. This is based on the idea that without a local market, long distance provides no service at all.

Finally, any proposed legislation must include an incentive or a penalty to prevent the bypass of interstate or intrastate telephone networks.

I am committed to making every effort to insure that every Indiana resident who desires reasonable access to telephone service will be able to obtain the service at a price which he or she can afford.

As a member of the National Governors Association, I have taken the opportunity to attach to my specific statement a copy of the Association's position which they will entertain in Portland, Maine, next week.

Again, thank you for your courtesy and the opportunity to express my opinion on this issue.

Chairman PACKWOOD. Governor, thank you.

We will follow the early bird rule of those who came first may ask questions first, and we will start with Congressman Bryant.

Representative BRYANT. Governor Orr, you referred in the first paragraph of your statement to past inaction by Congress which has allowed the tremendous confusion and uncertainty that exists to continue. Would you be specific about what area of inaction you are referring to?

Governor ORR. This has been something which has been out in the country being worked upon by local telephone companies. We are all aware of the decisions that were made, of the divestiture and deregulation, and it has seemed to me for a long time that this was an issue which might well have been brought to the forefront at some earlier point.

We are less than 6 months now from the date when this is all going to take place. Most telephone companies have spent a great deal of time trying to get themselves ready for all of this, recognizing that they had no other alternative.

I am simply glad that this process is being undertaken. As I said, it has seemed to me for some time that we should have proceeded earlier.

Representative BRYANT. Well, you said in the next paragraph that "because of past actions of the Federal Government through its judicial and administrative bodies, there is a potential that many segments of my constituency will be without telephone service." As I understand it, and I am as new as anybody in the room to the issue, we are here today principally because of the fact that the Federal antitrust laws were enforced against AT&T.

Do you have or does the Governors Association have some objection to the way those laws are written, or do you refer to something else?

Governor **Orr**. No; but what I am referring to is that decisions were made in the executive branch and judicial branch that have caused a process which is probably operating faster than everyone can keep up with to take place. I have no objection to the kind of action that is necessary under antitrust laws, but it seems to me in this case we are not able to keep pace with the situation, and that the public generally has not awakened to the seriousness of this issue. When it hits it is going to be a great surprise to everyone. I think it is high time we were working on it.

Chairman **Packwood**. Congressman Leland.

Representative **Leland**. Thank you, Mr. Chairman.

Governor, let me ask you. I noted in my opening statement that I was particularly concerned about the consumers who live on a fixed income, particularly our senior citizens and the unemployed. Let me ask if the Governors Association has made any decision or provided for any solution to this problem, given that these people are going to be the worst hit?

Governor **Orr**. There is concern about that, Congressman Leland. The National Governors Association has its annual meeting, as I indicated, in Portland, Maine, starting Sunday. There will be a discussion there. There has been little opportunity for the Governors Association to undertake these matters, although there has been conversation among us as to what elements of the population will be hardest hit. We will certainly do that.

Representative **Leland**. Now, of course, we have already drawn the analogy of the problem with natural gas deregulation and what that would mean if we do not come up with some solution. And I see too that you have drawn the same analogy in your statement.

Where on its scale of priorities, does the Governors Association place this issue?

Governor Orr. We have not as yet, but I would assume that it will be on the individual citizens 'priority list whichever bill reaches their mailbox first.

Representative **Leland**. Thank you, Governor.

Thank you, Mr. Chairman.

Chairman **Packwood**. Governor, do I understand you are saying that at the moment the National Governors Association has no position on a particular formula?

Governor **Orr**. We are going to be acting on that next week.

Chairman **Packwood**. But at least you are free to say that the Governors want to continue the present policy of some kind of universal service, which has been, frankly, paid for by long distance?

Governor **Orr**. I think that is generally true.

Chairman **Packwood**. Congressman Markey is gone. Senator Pressler.

Senator **Pressler**. My question is directed in the same way, as to whether, as we look at S. 1660, it would require that all providers of telephone service would be required to contribute to the new universal service fund. What is your view or the view of the Governors Association, I guess? If the Governors Association has not acted yet, I would have to ask for your view on the concept of including all service providers, including private systems, in the subsidy mechanism.

Governor ORR. Well, as I indicated in my testimony, there will be inequity among the States within the bill as to the degree of subsidy. In my opinion, in order to have any kind of a universal support among the Governors there will have to be some equity arrived at in terms of that subsidy, so that certain States will not bear the heaviest portion of the cost to the benefit of other States. That would be uppermost among the things that I am confident that the Governors will look at.

Senator PRESSLER. Going back to an earlier question, you were mentioning that this Congress has not acted quickly enough and that the Federal bureaucracy has not responded. Do you expect that the Governors will take a position on the antitrust law that was the root of this thing to begin with, Governor?

Governor ORR. I doubt that we will take that up as quickly as next week. It may be something to look at. Let me add that it seems to me that the Federal judiciary has also laid this upon all of us to be dealt with rather precipitously.

Chairman PACKWOOD. Chairman Dingell.

Chairman DINGELL. Mr. Chairman, I thank you.

Governor, we are delighted you are here. We will certainly keep your comments in mind. We thank you for your presence.

Governor ORR. Thank you.

Chairman PACKWOOD. Congressman Wyden.

Representative WYDEN. Thank you, Senator.

Governor Orr, is measured service one of the options being considered in Indiana at this point?

Governor ORR. Yes, with a good deal of objection on the part of a lot of people, and probably some degree of misunderstanding. Nonetheless, there is a great deal of noise and confusion on the subject of measured service, particularly from among that element of the population that you yourself identified, older people.

Representative WYDEN. Let me ask for your own personal feelings, because I know that the Governors are meeting, as you said. I am very concerned about the impact of measured service on the elderly. The phone is a lifeline. Many of them have nothing, literally, except the opportunity to talk with friends and neighbors, local associates, and try to figure out a way to have their problems resolved.

What is your feeling about the principle of measured service on the elderly and small business? Those are the two groups that concern me the most.

Governor ORR. At my request, our Public Service Commission is making an analysis of all of that. They are still in the process of doing so, still trying to reach a conclusion as to what effect measured service will have on various elements of the population in the entire system. I prefer not to have to answer that question, because I simply do not have that information at hand.

There is no question that the older citizens will be the hardest hit with measured service, and there is no question at this point that they have raised their voices the most loudly among the population.

Representative **Wyden**. Another quick question. You said that this problem is going to arrive on your desk later this year. You are going to send it back here because you think the problem—and I think correctly so—must be dealt with here.

But is it not going to be the position of the Governors Association that the States still want to regulate intrastate rates?

Governor **Orr**. Yes, I think that is appropriate.

Representative **Wyden**. Thank you.

Thank you, Mr. Chairman.

Chairman **Packwood**. Congressman Swift.

Representative **Swift**. Thank you, Mr. Chairman.

I could not agree with you more that it is terribly unfortunate that we have not taken action in this area before. Some of us, Mr. Chairman, Mr. Wirth, Chairman Dingell, Tom Tauke of Iowa, Tom Bliley, and I, and others, tried and got stomped about as hard as anybody can get stomped around this place by AT&T last year.

There is a relationship between public awareness and what in fact you can get done in this place, and the public awareness is increasing enormously and, as you suggest, it is going to increase a whole lot more when they get that first big phone bill.

But what you can do in the leadership you obviously intend to provide at the National Governors Conference, to get a strong statement from that group would be enormously helpful to those of us who do not intend to get stomped this time.

Governor **Orr**. Public pressure also motivates Governors, Congressman.

Chairman **Packwood**. Senator Gorton is gone. Senator Lautenberg.

Senator **Lautenberg**. Thank you, Mr. Chairman.

Governor Orr, I was interested in your remarks because they are in some ways similar to the view that I take.

You raised a delicate point, but one which cannot be avoided. You know that some of the subsidy plans before us would shift revenues and subsidies among States. You point out that Indiana would pay $4 to get back $1. My State of New Jersey, as a point of information here, would under one plan receive $1 for every 57 cents it contributes. Certainly that is not fair.

I support a Federal role in insuring universal service for those people with a low income who cannot otherwise afford basic service. But I would oppose playing one region, or one State, off against another by subsidizing everybody in high-cost areas and no one in low-cost areas, where rates may still be too high.

Instead, what I propose is a plan to help the poor, the elderly, the unemployed, again the modest-rate income or low-income people, whether they live in Kokomo or elsewhere, who cannot afford basic lifeline telephone service, that connection with the outside world. In some cases, as with the elderly, it is emotionally as well as functionally necessary to be able to communicate with family and those outside.

Do you support that kind of an approach, targeting on those individuals who need help because of their financial distress?

Governor **Orr**. There are other elements and constituencies that we all have which are going to be hard pressed as well—for example, a very large number of small business people who do not have any particular reason for making long distance telephone calls and therefore will get in effect lower charges or, as has been pointed out by the Senator from South Dakota, people in sparsely populated areas who will have a serious problem on their hands.

I think what we are all saying in another form is, this is the way it has been done, although nobody has actually realized it, over a long span of time, that there has been a subsidization through the Long-Lines charges. And what has struck everybody is very difficult to explain. I find it almost impossible to explain to people what is going on and why this is happening.

You can explain natural gas and blame it on the Algerians or somebody, but in this case trying to explain this, particularly to a senior citizen, is beyond anything I have ever attempted to do.

Senator LAUTENBERG. I think all of us sometimes wish we could put Humpty-Dumpty back together again.

Thank you.

Chairman PACKWOOD. Congressman Bates.

Representative BATES. Just getting back to the Governor's comments, I thought he was pretty hard on Congress for inaction, and yet I noted that the Governors and the PUC's and others have not taken action yet on this, and I hope they will.

The question I have, though, is with respect to your opposition to universal service, a universal service fund, which I think there is some merit to that if it is overdone in the terms of the subsidy. But if you would not support that concept, how do you hope to keep your farm rates in Indiana down?

Governor ORR. I think what I was driving at is that, as I understand them to be in some of the legislation that has been presented, there are inequities in terms of what portions each State would have to bear. I am not against the concept of the fund.

Representative BATES. But some mechanism of at least a transitional subsidy?

Governor ORR. Absolutely, and it would have to be some kind of a fund of that sort.

Representative BATES. OK. That was not clear to me.

Has the State of Indiana experienced rate hike requests?

Governor ORR. On telephone charges, yes, quite frequently.

Representative BATES. I mean since the divestiture issue. Do you have pending large rate hikes?

Governor ORR. There are pending large rate hikes. We have several telephone companies in addition to Indiana Bell, each of whom either have presented or are in the process of getting ready to present cases.

Representative BATES. Has Indiana Bell or the other companies—they do not have the measured service, I guess, that is now under study. Do they have a lifeline or some basic low——

Governor ORR. Not at this point. They have a measured service that is available to people. It has not been very widely used, however.

Representative BATES. If they had, as California does, a lifeline service for $7.50 a month, if they had something comparable to that, would that in your opinion be universal service, and would that then——

Governor ORR. It obviously would have to be subsidized by somebody, and I have not made an analysis nor am I aware that our Public Service Commission has.

Representative BATES. Thank you, thank you very much.

Chairman PACKWOOD. Congressman Whittaker.

Representative WHITTAKER. Thank you, Mr. Chairman.

Governor, would it be a fair characterization that essentially your testimony is that your criticism may be directed at the inaction of the Congress and that the effect of a rapid change or shift of burden to the consuming public is the primary concern of the Governors; and that, further, if we could achieve the dual goal of still opening the door to competitiveness in the telecommunications market, but do so at a gradual enough rate that the impact would not be severe on the consumer, phased in maybe over 5, 6, or 7 years, then we could maybe achieve the dual goals?

Governor ORR. It is entirely possible that it could happen that way, which is what I was aiming at when I raised the question of the speed with which all of this must take place. The point is, simply, that the public has been given very little opportunity to understand what is happening, and that there will be mistakes made simply because it must be implemented against such a close deadline.

Representative WHITTAKER. Thank you.

Chairman PACKWOOD. Senator Riegle.

Senator RIEGLE. Thank you, Mr. Chairman.

Governor, let me ask you, what do you think we should be shooting for as a monthly rate for people who are in the sort of hardship situation? Are we talking about, should we be shooting for $8 a month, $10 a month? Keep it under $10, $6? What would you say? What is your best hunch?

Governor ORR. I would hesitate to try to come to a number this morning. I have never attempted to make an analysis of it. I would be happy to take the matter up with our public service commission and see what a proper balance would be.

Our lowest rates in Indiana I think are slightly in advance of that, but I think someplace in the neighborhood of $10 or $11. So far I have not heard very many squawks on that level of monthly rate. But if it escalates and doubles, let us say, as has been indicated, or more, this is going to be a very big hardship on a lot of people.

Senator RIEGLE. So maybe something in the area of $10 a month would be just your initial reaction, recognizing again that you want to do more work on that and seek some advice on that?

Governor ORR. Let me go back to answering the question that I answered of Mr. Whittaker. The easing in of any kind of an increase is always somewhat easier than having an abrupt matter take place of this kind, particulary when there has been no preparation in anyone's mind for it.

Senator RIEGLE. In my State of Michigan, we have at present a lifeline type service that is available to all people and which allows them to place up to two calls per day. I think the monthly rate is $4 if they stay within the two call limit, and of course any additional local and long distance calls are added to the bill on a per call basis.

And as I understand it, there are about 300,000 people in my State who are on that system, which strikes me as a high number for such a limited service.

Do you have anything like that in Indiana?

Governor **Orr**. Not to my knowledge, although we do have a form of measured service where there are a certain number of telephone calls provided for within that charge. And my recollection is that charge is somewhere in the neighborhood of $12, $13 a month, varying I think throughout the State depending on the locality. My recollection is that theirs is something on the order of about 15 calls.

Senator **Riegle**. I just want to say, finally, that I agree with your point about not structuring a subsidy program in a way that some States are asked to carry an enormous burden to provide for support to some other State. Senator Lautenberg has expressed that concern and his bill reflects that concern.

But in some of the plans that have been proposed, Michigan, for example, would get a return of only $2 for every $10 that would be collected in the State and the remaining $8 would leave the State to go to subsidize service elsewhere in the country.

I think we have to avoid that kind of situation, and whatever mechanism we adopt is going to have to offer more equitable treatment State to State and region to region.

Governor **Orr**. If I may respond, in the national highway transportation system there has always existed some concept of donor-donee State. The very nature of population and geography brings that about.

I applaud the Congress in the action of last December in the Surface Transportation Act of bringing more equity.

Senator **Riegle**. We had to fight hard for that, as you know, and it did not come easy, and many States still did not get a dollar-for-dollar return.

Governor **Orr**. Yes, but it is a vast improvement.

Senator **Riegle**. I would hope that if some areas of the country or some States are going to need major subsidies, that rather than dump that burden on the more cost efficient States that may have other financial problems of their own, that we could develop a more equitable national system. However, if we need a subsidy for national purposes then perhaps it should be funded on a national basis, and the responsibility not be merely passed on to the States with little regard for each State's ability to support an adequate subsidy of its own.

I thank the chairman.

Chairman **Packwood**. Senator Ford.

Senator **Ford**. Thank you, Mr. Chairman.

Let me ask you a question about your statement. In it you refer to your party, and you would be a hypocrite to the philosophy of the party if you did not support the free market concept. The same paragraph, you said, "I am here today suggesting the national good requires boundaries to free enterprise, and particularly in this case."

Why is it so important here, and not to paint it with a broad brush, that you relate it to the free enterprise system that has all the competition?

Governor Orr. As I think I may have answered a comparable question from you, sir, when I appeared before the Energy and Natural Resources Committee——

Senator Ford. Your memory is about as good as mine.

Governor Orr. It seems to me in this situation that there needs to be a protection of the consumer for a period of time, but not permanently. There needs to be an easing in, so that there can be time given for all the considerations that need to be undertaken, as well as to simply ease the financial pressure.

Senator Ford. So you are saying that you want a phased-in situation rather than an abrupt change?

Governor Orr. Yes.

Senator Ford. In your next paragraph you also say that we must be willing to provide basic telephone service at a price below actual cost. How are you going to ask private enterprise to provide service below actual cost unless they are able or we as an institution tax or work out some other system here to collect some money to put in the pot to give to somebody else? How else can we do it?

Governor Orr. We were doing it as a nation by the subsidy provided by long distance charges.

Senator Ford. OK. But we could not get an answer from AT&T as to what that charge was back then. Now we know they were charging an excessive amount for long distance, and they were subsidizing residential rates. But back then we could not get the facts and the figures and the documentation, which somehow, lo and behold, has arrived.

Now, as January approaches, AT&T is going to be broken up and we need more money. Your State is getting big ones and so is mine. They have been subsidizing residential rates. It is a surprise. It abruptly was brought before us where we could see it.

Governor Orr. We learn a good many things as we go along, Senator, I agree. And I think in this case there needs to be temporarily a period of time—I am not here to indicate exactly how long. That is something I think that comes out of hearings and deliberations in the Congress. I think that there needs to be an easing into whatever the new period might be, and I believe under those circumstances we will see the free market system work effectively.

Senator Ford. How can we initially, then, work out a system so that we can provide telephone service at below actual cost?

Governor Orr. Only through some kind of subsidization.

Senator Ford. Either from industry or from the Government as it relates to the charge?

Governor Orr. Presumably, those that are likely to be benefiting on one side of the issue would be those who would be subsidizing on the other side.

Senator Ford. That is right, those who have given to those who have not.

Governor Orr. On a temporary basis.

Chairman Packwood. Senator Danforth.

Senator Danforth. Governor, you have talked about the coming public reaction to very high increases in telephone bills. We in the Congress deal with a large part of the problem when we deal with cross-subsidies, with access charges, and with the principle of universal service. We cannot, however, deal with absolutely holding people harmless against any rate increases at all.

It seems to me as we enter into this consideration that it is important not to overpromise what we in the Congress can do. Even those of us who support Senator Packwood's bill would not want to represent that there is going to be a total freeze on telephone rates or services, just as there is not a total freeze on anything else in the economy.

Is it your view that the coming uproar would be resolved by mitigating the very rapid projected increases of phone costs, or would it be necessary to hold people absolutely harmless against any increases?

Governor **Orr**. I think it is a temporary situation more than it is one of the long term, and I think it would be probably improper to hold harmless, and it certainly is wrong to hold that out as a likelihood.

It is, in my opinion, in the interest of the public, and in the interest of the workings of government, to ease this situation which stares us in the face. My plea is that we recognize that fact and take effective action so that it will not be something that besets the Nation all of a sudden and that it will not be something that creates a very serious problem, let us say, from the standpoint of our economic recovery.

That was also one of my pleas so far as the natural gas situation was concerned. It is something which this coming winter is going to be more serious than the previous winter, simply because the weather is likely to be colder, and we have a combination of all of these factors, to say nothing of cost increases in electric rates. The consuming public will most certainly make their point of view known.

Senator **Danforth**. Thank you.

Chairman **Packwood**. Congressman Oxley.

Representative **Oxley**. Thank you, Mr. Chairman.

Governor, the average telephone bill in this country is $11 a month, and the chairman of the House Telecommunications Subcommittee, as well as other people, have estimated that over the next decade those basic rates will probably double. Does that strike you as excessive?

In the near term, that is an average of $11 a month. Does that progression to doubling, say to $22 in the next 10 years, strike you as particularly excessive?

Governor **Orr**. I think it will depend a great deal upon inflation. There are a great many costs that we have experienced today that are constantly surprises to us because of the fact that they are double what they were 10 years ago.

Representative **Oxley**. A lot of those, almost all of them.

Governor **Orr**. But we experienced unusually high inflationary conditions during a good deal of that period of time. If we are able to throttle inflation, I would question whether those figures would be accurate. But I have no means by which to know what the costs of the equipment and things of that kind, as well as the advance in technology, might add to the burden.

Representative **Oxley**. Well, does the cost of telephone service where you can have a telephone in your house and reach almost anyplace in the world at a cost of 30 cents a day, strike you as excessive?

Governor ORR. No. As a matter of fact, there have been many comparisons drawn between the services provided by the telephone companies, both basic service and long distance over the years, and the cost to the public of the U.S. Postal Service. In every instance, the telephone industry has shown like a giant by comparison to the U.S. Postal Service's efforts to stay alive with unbelievable increases in costs to the consumer.

I think what we are looking at is a situation, as I have said before, where divestiture is bringing about changes being made very, very rapidly, where unfortunately I believe there could be some mistakes made, but, in addition to everything else, enough time allowed in which to readjust to the kinds of free flow of the market that can help to bring some costs in line.

Representative OXLEY. Thank you, Governor.

Chairman PACKWOOD. Senator Gorton, do you have any questions?

Senator GORTON. No questions.

Chairman PACKWOOD. Governor, thank you very much. You were very patient to stay this long.

Governor ORR. I appreciate greatly your interest and wish you well.

Chairman PACKWOOD. Thank you.

Governor ORR. We understand that 50 Governors have equally as much difficulty in controlling the costs of various utilities as this Congress.

Chairman PACKWOOD. Well, I would be surprised if 50 Governors could come up with one formula which will satisfy them all.

[The statement follows:]

STATEMENT OF HON. ROBERT D. ORR, GOVERNOR OF INDIANA ON BEHALF OF THE NATIONAL GOVERNORS' ASSOCIATION

On behalf of the State of Indiana and my fellow Governors throughout the Nation, I deeply appreciate the opportunity to present these comments to the honorable members of this historic joint hearing on universal telephone service legislation. The issue of assuring quality, affordable telephone service to all American citizens demands the highest attention of the Congress. I strongly endorse your recognition of the immediacy and the magnitude of the problem. I also applaud the expedited and unified approach by which you are seeking to fashion an adequate statutory solution. Past inaction by Congress has allowed the tremendous confusion and uncertainty that exists to continue.

Because of past actions of the Federal Government, through its judicial and administrative bodies, there is a potential that many segments of my constituency will be without telephone service. Today my concern is for the elderly, the indigent, the small businessman and rural phone users who face the prospect of bearing the so-called full cost of local service. My Hoosier constituents are not yet as aware of the telephone issue as they are with the natural gas issue. But, I can assure you that as soon as that first phone bill comes in they will be camping on my doorstep. I'm here to let you know, and to let them know, that the problem has to be dealt with here. My hands are tied. Congress must act, and act quickly, to regain control of this situation and prevent these serious problems from occurring.

Parenthetically, let me add that Natural gas is still as important an issue as it was when I testified before the Senate Energy and Natural Resources Committee last spring. Congress apparently is not going to act on that serious matter. In my opinion, this is an inexcusable dereliction of duty.

We are now 3 months closer to the date when natural gas bills go through the ceiling again once frigid weather hits us next winter and consumers begin howling once more—and with ample justification.

You and your collegues need to be worrying that escalating natural gas bills and sudden large increases in phone bills will arrive in people's mailboxes simultaneously.

Congress has loosened the regulatory bonds which kept the free market from working its will in the communications industry. And in turn, this has permitted the introduction of products and services which have truly advanced the science and business of electronic communication. As a Republican Governor, I would be a hypocrite to the philosophy of my party to decry the good effects of free market economics; the freer the market, the more efficient the allocation of goods and services. In the case of telephone service, as with nearly every segment of our economy, national policy must dictate the boundaries of the free market. I am here today to suggest the national good requires boundaries to free enterprise in this case. And to support, in principle, an acceptable middle ground in this question of deregulation, let us have fair competition. Let us not have a cost-based pricing system which destroys the concept of universal service.

This nation has the widest proliferation and saturation of telephone service in the world. This provides a communication network that is second to none, and is of national significance beyond the specific benefits enjoyed by the individual user. We must not create barriers which reduce access to this network, for that reduces the value of the network to everyone. In short, if necessary we must be willing to provide basic telephone service at a price below its actual cost.

I am not, however, prepared to support any specific proposal for a national universal service fund created by charging long distance carriers to help defray the cost of local services. This is based on the idea that without a local market, long distance provides no service at all. I accept the fact that Indiana residents will gain by having a policy that assures universal access in all States. I am concerned that, according to information provided to me, the national universal service fund provided by some of the proposals would result in Indiana telephone users contributing no less than $12 million to other States. We would receive approximately $1 in return for every $4 we contributed. Expanding that same analysis to five Midwestern States, (Ohio, Michigan, Wisconsin, Illinois, and Indiana) the net outflow of revenue to help support telephone services in other parts of the country would be in excess of $80 million. I have serious reservations about that level of interstate transfers of revenue.

I must take a strong position that, in addition to providing universal service availability, Federal legislation on this issue must also provide clear statutory responsibility for State control of intrastate telephone rates. By doing so you can provide a means for States to assist in providing additional relief, if required, to the provision of local services, and thereby perhaps minimize the degree of subsidy required at the national level.

Finally, any proposed legislation must include either an incentive or a penalty to prevent the bypassing of the interstate telephone network.

I am committed to making every effort to insure that every Indiana resident who desires reasonable access to telephone service will be able to obtain that service at a price which he can afford.

As a member of the National Governors' Association, I have taken the opportunity to attach to my specific statement, a copy of the Association's position.

Again, thank you for your courtesy and an opportunity to express my position on this issue.

ADOPTED BY NGA COMMITTEE ON TRANSPORTATION, COMMERCE AND TECHNOLOGY—AUGUST 1983

COMMUNICATIONS

The National Governors' Association urges Congress to review national telecommunications policy. NGA supports timely revision of the Federal Communications Act of 1934 to reflect the following concerns:

1. Reaffirm the original purpose of the act, giving priority to the objective of providing universal telephone service on a basis that ensures high-quality service at reasonable rates to the users of residential telephone service.
2. Provide for the design and management of the nationwide telecommunications network as a unified national resource with emphasis on maintaining quality services to all areas of the country at reasonable rates.
3. Provide that future technological advances in telecommunications be made available to all classes of customers and to all areas of the country whenever possible.

4. Provide for more effective participation by state regulatory commissions in the development of telecommunications policy, particularly as it relates to all matters affecting residential and local exchange services.

The Governors urge Congress and the Administration to closely monitor the effects of the divestiture of AT&T to provide for the equitable and timely implementation of the settlement agreement; to ensure that high quality universal telephone service is available to all areas of the country at reasonable rates and that a healthy competitive environment is promoted in the telecommunications industry.

5. Provide for a strong role for the states and local governments in regulating the cable television industry to ensure quality service at reasonable rates to subscribers.

NGA opposes premption by the federal government of state and local authority to regulate the cable television industry through their intrastate common carrier and franchising powers.

The cable industry has not demonstrated that current state and local regulations have restrained its ability to grow and earn a reasonable profit. No individual segment of the telecommunications industry should have significant economic advantage over the competing interests. The Governors believe that federal preemption of state authority should be adopted only as a last resort.

Chairman **Packwood**. Next we will hear from the Chairman of the Federal Communications Commission, Hon. Mark Fowler. Mr. Chairman.

STATEMENT OF HON. MARK FOWLER, CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION, ACCOMPANIED BY JACK D. SMITH, CHIEF, COMMON CARRIER BUREAU; AND CARL D. LAWSON, ACTING CHIEF, POLICY AND PLANNING DIVISION

Mr. **Fowler**. Mr. Chairman and members of the committees: I welcome the opportunity to appear before you today to address our mutual concerns about the affordability of telephone services, the continued health and vitality of the telecommunications industry, and the social and business activities which rely upon telecommunications.

With me today, on my right, is Jack D. Smith, Chief of our Common Carrier Bureau; and on my left, Carl D. Lawson, who is Acting Chief of the Bureau's Policy and Planning Division.

In my prepared testimony, which with your permission I will be submitting for the hearing record, I go into detail on the importance of emerging policies in this ever-changing industry, and I address the specifics of the FCC's access charge decision as we defined it yesterday. I highlight the concomitant changes in the jurisdictional separations being considered cooperatively by the FCC and by the state commissioners on the Joint Board, and I discuss my concerns regarding possibly undesirable effects of various legislative proposals that are now being considered.

I will not repeat these detailed comments now, Mr. Chairman. Rather, my oral remarks I would like to use to emphasize five main points:

Point No. 1, first, that the FCC is committed to achievement of the same goals as are expressed in the various bills that are before you right now. Any differences relate solely to the means of achieving these goals and not to the goals themselves.

The touchstone of the Commission's treatment of access charges and related matters is the Communications Act, a directive from Congress which wisely states the multiple objectives that telecommunications service should be available "so far as possible to all the people of the United States" and should be "a rapid, efficient, nationwide service, with adequate facilities at reasonable charges."

We take these objectives very seriously. In formulating our access charge and related jurisdictional separations proposals being fashioned in cooperation with the States, we have carefully sought to achieve an appropriate balancing among these somewhat competing objectives.

Second, the genesis of the various bills before you is the concern that the rate hikes now being sought for state-regulated telephone services will increase the price of telephone service so much that many subscribers will be forced to discontinue service. While we too are committed to avoiding any such result, in our decisions we have taken into account rate impacts on all consumers and we fashioned long transition plans to insure against rate shock.

Moreover, yesterday, in response to concerns articulated by the State of Michigan, we instituted an investigation to examine comprehensively the facts surrounding the recent rash of proposed telephone rate increases in the States. We will release a report on this issue before the end of the year. Thus, if further actions appear warranted to alleviate an impact from our decisions, we will be in a position to act and act quickly.

We also reviewed our access charge decision yesterday and further eased the transition, thereby eliminating the end user usage charges which had been contemplated and reducing the flat charge upon residential users from a minimum $2 in the first year per month to a maximum $2 for the year 1984.

Thus, it should be apparent that the access charge decision will have only a minimal effect upon consumers and there will be no excuse for the large rate hikes sought before many state regulatory bodies. It should be obvious, for example, that the Commission's $2 access charge cannot be used as justification for the $20 rate hike that Southwestern Bell is seeking in Texas.

Accordingly, I would recommend that Congress stay its hand until it can review the results of our yearend investigation of the State rate situation. If corrective action appears warranted, then it can be enacted during 1984, when the actual effect upon subscribers will be $2 a month or about 7 cents a day.

What is at issue here is how to split the cost of telephone service between long-distance and local service, the cost of the loops and the wires and the terminal equipment that the subscriber uses. In other words, what I am basically talking about is the wire that goes from the business or home to the telephone office.

In the past, the recovery of these costs has been buried in long distance rates. What we are trying, through the access charge decisions, is to expose those costs to view so that each person who benefits from the use of these facilities will pay their costs alone.

The access charge plan will yield significant benefits to the public and our country in the form of reduced long distance rates. It may gain greater acceptance across the country than many current critics would suppose. We believe that the plan provides the foundation for this country's growth into a very new and exciting, we think, and promising information age, and will stimulate communication activity and will create thousands of more jobs, spawn countless new industries, and improve greatly our national productivity and international trade position.

No. 3, the FCC is committed to a careful monitoring of the potential and the actual effects of access charges on the relative universality of telephone service, which as I said at the beginning of my testimony is the goal that we too share. We have adopted phasing-in procedures over a 6-year period which will facilitate this monitoring, and we retain the flexibility to refine or modify the plan if undesirable effects occur on the wide availability of telephone service, on competition, or on service efficiency.

The telecommunications industry is fast changing and dynamic, and new technologies and service offerings are the everyday norm. Flexibility is absolutely required, because without it the industry may be artificially restricted, depriving the people of our country of many enormous benefits which otherwise will be realized.

Fourth, as I am sure you recognize, regulatory initiatives such as the legislative proposals under consideration today must be consciously sought out to avoid any unintended effects or results. Since legislation, once in place, is very difficult to offer, all the more care we believe must be given to insure that the legislation is workable and sound from both the shortrun and long-term perspectives.

We would caution against proposals which are too heavily weighed in favor of maintaining current rates and service arrangements, which might thereby inhibit the natural and dynamic growth industries and tendencies in our magnificent telecommunications industry.

Alternatives to carriers' offerings have long been available to subscribers and they have benefited from these many alternatives. I am speaking here of alternatives such as private microwave systems, domestic satellites, cellular and land mobile radio, new point to multipoint uses of excess capacity on broadcast facilities, and of course cable and optical fiber transmission systems.

We believe that the benefits of new entry, competition, and consumer choice should not be ignored or penalized in favor of inefficient pricing systems. The cost of such a policy on the domestic economy and on the international competitiveness of the United States is simply too high.

Last, it is important to recognize that the FCC's access charge plan does address the very goals which are at the heart of the several bills before you. Telephone service in high-cost areas, typically rural areas, will be supported under the access charge plan and under cooperative Federal and State regulatory procedures which have been recommended by a Federal-State joint board.

Phase-in procedures to minimize dislocations to residential subscribers are in place and will be carefully monitored to insure that the wide availability of telephone service is not affected. A decrease in long distance usage charges will be brought about by the movement toward equality of access payments by other common carriers, by use of surrogate surcharges on private lines, and by short phase-in procedures for business subscriber access charges.

Importantly, the access charge plan also establishes a procedure whereby exchange carriers can seek waiver of the subscriber's flat charges in order to accommodate lifeline type services. Thus, States will be able to maintain targeted support of telephone services for the poor and the elderly and others who would otherwise be unable to continue the service.

In summation, I would observe that the bills before you will not cure the difficult problems which are perceived as a result of proposed telephone rates around the country. Telephone rates may be increasing, but the access charge plan is not the principal reason, and reversal of that plan would not cause these increases to evaporate.

We would also urge caution to insure that any legislation adopted not diminish the benefits of competition, innovation, new entry, and efficiency which are being realized to an ever-increasing degree. In any event, we certainly recognize that ultimately the policy is in the hands of the Congress and not of the Federal Communications Commission. I would hope that the Congress would carefully consider at this time whether any legislative remedy is warranted.

If you do ultimately decide that one is warranted, we, of course would offer the services of our Commission and staff to assist you in any manner you see fit.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Thank you, Mr. Chairman.

Several people have asked what our plans are about lunch. I have talked with Chairman Dingell. We will meet right through lunch in the hopes of finishing up by about 2 o'clock this afternoon.

Following again our early bird rule, Congressman Bryant has returned from his vote and he is first up.

Representative BRYANT. Thank you, Chairman Fowler.

I wanted to ask you first if it is or is not true that under existing network configurations the local operating companies provide AT&T with an access to the local exchange which is superior in quality to the access provided to AT&T's long distance competition?

Mr. FOWLER. Yes, that is true, and it has been recognized.

Representative BRYANT. I also understand that this superior interconnection enables the local operating companies to provide additional services to AT&T and enables AT&T to provide additional services to its subscribers. Could you describe some of those benefits they receive by means of that superior interconnection?

Mr. FOWLER. Excuse me a second here, sir.

I will ask Jack Smith to handle this.

Mr. SMITH. I think you are referring to the differences in interconnection between what the other common carriers receive and what AT&T receives.

Representative BRYANT. That is right.

Mr. SMITH. The differences include things like MCI, for example, is considered another common carrier. They might have to dial 22 numbers if you are a customer using MCI service to get long-distance, a long-distance number, while you might only have to dial 9 numbers to use AT&T. Is that the kind of differences you are speaking of?

Representative BRYANT. Yes, there are others, are there not?

Mr. SMITH. Yes, answer supervision that AT&T would get and that the OCC's would not get, and there are other differences in interconnection which do contribute to AT&T having what we have considered to be a premium interconnection over what the OCC's get.

Representative BRYANT. In terms of competition for long distance, the advantage there would translate into substantial value for AT&T, would it not?

Mr. FOWLER. Yes, indeed, sir. And in our access charge decision we specified that AT&T has to pay more because of those differences for the interconnection.

Representative BRYANT. I have no more questions. Thank you.

Chairman PACKWOOD. Congressman Leland.

Representative LELAND. Thank you, Mr. Chairman.

Mr. Fowler, there has been much discussion about whether the FCC's access charge plan is an economically efficient pricing scheme. But won't the value of the telephone network decline if consumers are unable to pay the flat charge and leave the network? Doesn't universal service have a very real economic value to our largest telephone users, and should they not pay for assuring continued universal service?

Mr. FOWLER. I certainly agree with you, Mr. Leland, that universal service is very important. And yes, obviously the value to each subscriber of the network is enhanced to the extent that we have true universal service, that is, the greatest number of people on the network. So I certainly agree with that.

What we are attempting to do, what we have tried to do in our access charge decision, is to make sure that universal service is protected through our universal service fund, through our monitoring efforts, through a very long transition that goes through 1989, and with a decision to be made as a safety valve in 1986 as to whether we want to go forward with the transition further or whether we want to evaluate everything at that time, plus provisions providing for lifeline services if the States apply for waivers.

In addition, so that we make sure that we will continue to have universal service, that transition period can give the Congress the time it needs, should we need to establish a fund to target poor people or elderly people. As the access charge schedule proceeds, it will give the Congress time to set up that fund and target those needy individuals, as you yourself I think had observed when you had joined in introducing certain legislation which you spoke of earlier.

So we make sure that subsidies are not being visited on everyone, whether they need it or not, which is our present system, but rather that we make sure that people who really do need those assistances will be able to get them.

Representative LELAND. What effect would the FCC's access charge order have on the total telephone bill paid by subscribers?

Mr. FOWLER. Well, we have specified a schedule of changes. In 1984 it would provide for an end-user charge, flat charge of $2 per month. That goes to $3 in 1985, and then it goes to $4 in 1986.

But in 1986 we have specified that we will then look at what has happened and the impact of this, before deciding whether we are going to proceed further. It ultimately winds up a total of $6 at the end of 1989, so that in 1987, 1988, and 1989, if we were at $4 in 1986 you would do a third of $2 in 1987, increase a third in 1988, and a third in 1989.

So that in 1989, assuming that we had found that in 1986 there was no undue impact on the universal service, we would have a $6 flat charge. But long-distance rates, I should add, we estimate would be down about 35 to 40 percent.

Representative **Leland**. One last question. What studies has the Commission done to identify those who would gain under this plan and those who would lose?

Mr. **Fowler**. Carl, do you want to answer that? Maybe Tom might want to.

Mr. **Lawson**. I do not believe that there is a study specifically of who gains or loses in terms of telephone rates themselves. I think the underlying assumption is that the distortions from departing from what the economics would dictate impose indirect costs throughout the economy, and that the country as a whole would benefit by getting to cost-based pricing.

Representative **Leland**. Thank you, Mr. Chairman.

Chairman **Packwood**. Very quickly, Mr. Chairman, the figure is normally bandied about of $9 billion or $10 billion as the present surcharge on long distance, if you want to call it that, that is then used to subsidize residential and rural rates. Is that roughly an accurate figure?

Mr. **Fowler**. You are talking about the subsidy on long distance?

Chairman **Packwood**. Yes.

Mr. **Fowler**. It is about, I believe, $11 billion, $10.7 billion.

Chairman **Packwood**. Now, in your statement you indicate the Federal Communications Commission acts under a congressional mandate, and you read the directive, "to provide service so far as possible to all the people of the United States," and "it should be a rapid, efficient, nationwide service with adequate facilities at reasonable charges," correct?

Mr. **Fowler**. Yes, sir.

Chairman **Packwood**. And indeed, you are a creature of Congress and you are to attempt to administer in this case the telephone laws in accordance with what you think Congress has intended.

Mr. **Fowler**. With true fidelity, yes, sir.

Chairman **Packwood**. Is it also true that the consent decree between AT&T and the Justice Department has nothing to do with your long-distance charges?

Mr. **Fowler**. You mean with the access charge decision?

Chairman **Packwood**. You can put the access charge in if you want. But the consent decree in no way limits your ability to decide what you are going to charge for long distance?

Mr. **Fowler**. Yes, sir.

Chairman **Packwood**. So that any allegation that the rates are going up or going down, long-distance rates, because of the consent decree is simply a misplaced allegation?

Mr. **Fowler**. Largely that is so, yes, sir.

Chairman **Packwood**. Now, for years you have followed this policy of subsidizing rural and residential rates with long-distance charges, acting on what you thought was Congress mandate, and Congress never said anything. We seemed reasonably happy with it.

What has given you the impression that Congress has changed its mind as to what we want you to do?

Mr. **Fowler**. That is a very good question, Mr. Chairman. I probably should engage in just a little history here. Back after the Second World War, as the costs of local service started to rise—we had some inflation at that time—a decision was made by the regulators, who were then at the FCC and the State people, to begin to hold local service down, which essentially had been the flat rate which had been paid back then and essentially took care of the cost of local service.

They started to load more of a subsidy on to long distance, and they were able to do this and essentially, if you will, get away with it for years and years and years, because technologies kept driving the costs of long-distance service down. So you could continue to load more subsidies on to local service.

But what has happened, beginning in the late, perhaps in the midseventies—we are not exactly sure when, but increasingly so, certainly, now in the early eighties—is that with these gigantic subsidies that were built up or created over a period of time on long distance, up to about, I guess 15 cents a minute now that you pay on both ends when you make long-distance calls in the form of a subsidy, that goes to help other folks keep their local service down. With new technologies coming on board that were very efficient, businesses and other large users of the great long-distance network said, hey, what we are going to do is construct systems here, because we can do this a lot more cheaply than carrying this tremendous subsidy now that is built into the long-distance rates.

So we got into a very real concern about bypass, where you set up alternative systems to bypass the local exchange and thereby escape paying the subsidy. And I believe—and the evidence, although admittedly it is anecdotal—we see instance after instance of gigantic systems either being planned for now by businesses or actually under construction, particularly in large major cities, where they are bypassing the local exchange and avoiding having to pay those subsidies.

Chairman **Packwood**. Could not your policy just as well have been that we will bring into the system those that are attempting to bypass it and continue the subsidy?

Mr. **Fowler**. I just want to say one thing before I answer that, sir. Had we not acted, we believe, if they go off the network and do not pay that subsidy over a period of time, it is apparent to us that we will wind up with all of those costs still having to be paid by the folks who remain on the network, and in turn that will drive more businesses off the network. And we could wind up down the road with a network that is very seriously injured or affected, and maybe even seriously impaired, maybe even threatened.

Now, your question is, could you somehow prevent them from going off?

Chairman **Packwood**. Well, if not prevent them from going off, simply finding a way to charge them even when they are off. Call it a spectrum fee, call it what you want. The fact that they go off the wire does not necessarily mean they are beyond your reach.

Mr. **Fowler**. Yes, I understand that. I think you have got to be careful when you do that, sir, because I am thinking of some of the technologies that have come about as a result of new technologies.

For example, a lot of companies have had private microwave systems that they have built that are very efficient. General Motors is one, for example, that has made great use of a private system, and others, to hold their costs down.

If you load too much of a tax, or whatever you want to call it, on that, you may discourage the implementation of economically efficient means of private communication or new technologies. In effect, what you are doing is, if the tax is sufficiently large, precluding bypass, but also discouraging the introduction of new technologies.

And I think that means that you then give a monopoly to the local exchange, and there is nothing competing with it to provide service on a local basis there that is through new technologies which may be more efficient and ultimately can keep the costs of goods and services that our people pay for down much further.

Chairman **PACKWOOD**. Let me ask this one question. I am over my time.

Did anybody from Congress come and talk to you, however, and say, we want to get rid of this old system we have had where we have subsidized residential and rural rates with long distance? Did Chairman Dingell or Chairman Wirth or Chairman Goldwater or Senator Ford come and say we think the system we have used for a good many years ought to be changed?

Mr. **FOWLER**. No, sir, nobody did one way or the other. But I do believe, and indeed the entire Commission felt, the three Democrats and four Republicans, unanimously believed that had we not acted we ran the risk of seeing the destruction of our great national network, as more and more companies got off the system.

And they are the ones, because of their great use, that have provided the greatest support for that system through the revenues that have been charged to them.

Chairman **PACKWOOD**. Congressman Markey.

Representative **MARKEY**. Thank you, Mr. Chairman.

Mr. Chairman, how do you see a subsidized lifeline service rate as an answer to the problems that the urban poor, the elderly, the disadvantaged, face their very real difficulties in attempting to pay for their phone bills? If the national average for phone bills is $20 a month, subsidies to limit rates to $30 a month in high-cost areas do little to help those who cannot afford even the first $20, don't they?

So would you agree that some additional mechanism, like lifeline service, will be required to help protect those people at the lower end of the economic spectrum?

Mr. **FOWLER**. Mr. Markey, that is certainly one option, a lifeline service, and that could be also offered in conjunction with a targeted subsidy, which I spoke to Mr. Leland about earlier, to assure that those people can have service.

Also, there is a possibility of measured local service as well. So there are some options there, because we want to make sure that all of the people in our country are able to have telephone service.

Representative **MARKEY**. So are you seriously looking at measures to encourage lifeline services?

Mr. **FOWLER**. Well, we are providing that the States, if they want waivers of the flat charge provisions, may seek them in order to permit needy people to be able to have lifeline service and not have the end charge put on them.

Representative MARKEY. Thank you. Now, a number of rural telephone companies oppose the Joint Board's plan and argue that there ought to be more of a subsidy to rural areas. A number of the bills also propose a larger subsidy to rural companies.

My bill, as you know, adopts the Joint Board's subsidy formula. But what would such a larger subsidy, such as that proposed in S. 1660, actually cost? Who would pay for the subsidy?

Mr. FOWLER. That would again be a subsidy on long distance. It would be loaded on long distance, and we think that is right. And we provided for that, sir, in our decision. We had the universal service fund, which is specifically designed to kick in any time the costs of telephone service, the average, is 15 percent above the national average.

So that we can protect those rural, typically high-cost service areas from undue increases which otherwise would occur. We think that is a good national policy. That is about 2 cents a minute that we think it would be good national policy to continue to have the long distance users pay to protect the rural subscribers.

Chairman DINGELL. Would the gentleman yield to me?

And I thank him, and I will yield him some of my time.

Mr. Chairman, isn't the FCC's program just moving a large part of the charges from the long distance users under circumstances which will increase local access charges, and actually encourage bypass?

Mr. FOWLER. No, sir.

Chairman DINGELL. I must respectfully differ. But I thank the gentleman for yielding.

Mr. FOWLER. We do not think that will be the case. Right now we have folks, when they use their long-distance phone and talk for 10 minutes, they pay $1.50 to another fellow down the street for that local line that goes from his house to the central office even if he does not make any long-distance phone calls that month, never mind whether he is needy or not.

What we are saying is, does it not make more sense to bring that subsidy out so that he pays what you pay for long distance and vice versa and he pays what you pay for his loop from his house to the central office. And for those who cannot afford, we do need, clearly, to have a targeted subsidy. And that money could be a fairly reasonably sum, we hope, and a lot less than the kinds of money we are imposing now on the long-distance system.

I guess what we are saying is that if you can eliminate that subsidy, that hefty load on long distance, there are going to be a lot of initial benefits. We are going to see lower priced goods and services, people brought closer together because more phone calls are made, lower long-distance rates—we estimate at the end of 1989 35 to 40 percent—the creation of new businesses and industries, more computers talking to computers, the creation of new jobs, which is important to our country and to our American men and women.

And it goes directly to the kind of life they are going to have. It will increase productivity because businesses will be able to make better use of long distance for marketing. Instead of sending salesmen out, you can have telemarketing. Small businesses will be able to use computers to tap into data banks and do things that small businesses cannot do now, because it will be cheaper to do it.

Businesses will have more flexibility in where they locate. I wish that Senator Pressler was still here, because that means they can locate in his State much more easily now because long distance puts them in touch with everywhere they need to go.

It will also improve our international trade position and I think also strengthen our domestic industries against international competitors operating in our domestic market. And all of that because we are shifting a modest cost, which most pay anyway in long distance over to the true user, that is, the fellow who is having that wire dedicated to his use.

Again, as Mr. Markey and Mr. Leland particularly have talked about, it is also possible to preserve the universal service through the targeted subsidies mechanism.

Representative MARKEY. Mr. Chairman, could I ask unanimous consent to ask one additional question, so I will not have lost my thread of thought?

Do you believe that the Joint Board action needs to be further modified to give additional help to rural users, or do you believe that what has already happened is adequate? And if not, will not the additional help put a real burden on those urban users in trying to make that additional aid?

Mr. FOWLER. It is a good question, sir, and we agonized together, the four State members and three Federal members, as to what the appropriate level was. We concluded that if it was a 15-percent figure over the national average cost, then that is when the subsidies would kick in.

We built in a margin of about 15 percent to give the rural companies an incentive to be efficient. With that 15-percent margin, they would still be efficient. Otherwise, if the subsidy kicks in immediately, we felt that they would have no incentive to be efficient and you would have your so-called gold-plated systems.

One member, I know, felt that perhaps a 10-percent over the national average cost would be the appropriate figure. But we basically then agreed that the appropriate figure was 15 percent.

Representative MARKEY. So you think the board's action was adequate?

Mr. FOWLER. It is, and I think, of course, reasonable men can differ on that number, sir. I recognize that. But we figure if the company's cost were 10 percent above the national average the difference in dollars was incredibly larger. It was very, very significant, and we felt that it put it into a area where perhaps we were providing subsidies when they really might not be needed and loading a much heavier subsidy again on the long-distance users.

So we felt we cut it about right, but it was a difficult and long decision. It took us a long time to reach that.

Representative MARKEY. Thank you very much, Mr. Chairman.

Chairman PACKWOOD. Chairman Dingell.

Chairman DINGELL. Chairman Fowler, thank you for being here. Under the Commission's reconsidered access charge decisions, are all NTS costs ultimately shifted to the end-user in the form of flat charges?

Mr. **Fowler**. All of the NTS costs that have been borne through long distance usage, yes, sir.

Chairman **Dingell**. They are.

Mr. **Fowler**. We do not have any jurisdiction over what the States might do as to their share.

Chairman **Dingell**. Now, since that is the case, I wish you to know that I still fundamentally disagree. Let me read to you some of Judge Green's views on your access charge decision.

> This decision undermines one of the assumptions underlying the court's approval of the decree, that there would be no impairment of the principle of universal service.

Judge Green also stated, and I quote again,

> Ninety-one percent of all households now have telephones. As the FCC's access fee reaches $7, as it will in a few years, this is estimated to drop to 60 percent for very poor blacks, 65 percent for very poor living in rural areas, 58 percent for poor young people.

This hardly sounds like universal service.

Now, in view of the judge's concern, which I share very strongly, what is the justification for loading all NTS costs on local customers?

Mr. **Fowler**. The justification is very simple, sir, and I want to just make this clear, because it is a complicated area, but I will just simplify it. It helps me. You have a wire that runs from a business or a house to the telephone office, and that comprises about 45 billion dollars' worth of costs right now over the whole country. Someone has to pay for that, and the question is, Who should pay for it? In the past what we have done is say, if you use long distance, you can take that subsidy and use that to pay for at least the Federal portion of those costs, which has amounted to about 15 cents a minute.

The problem is, when you do that, you are taxing in effect folks who do not get the benefit of the other fellow's wire. If you make long-distance calls, six or more average-length long-distance calls, you are providing subsidies to somebody else locally or wherever he is. Somebody else is receiving that benefit, and he may or may not need that subsidy, but he simply does not make very many long-distance calls.

So, you are taxing someone or charging for use he does not receive, or a benefit he cannot get, and taking the subsidy and giving it to people who may not need it. So we think that the better way in view of all of the benefits that we think will accrue that I talked about earlier to our country by limiting that subsidy would be to say, OK, you pay for the wire that goes from your house or business to the central office, and we are going to do it on a very gradual basis. We are going to start with $2 a month, and we are going to phase it in over 6 years, up to $6 over 6 years.

In 1986, we are going to look at it when we are at $4 to make sure that it is still working and there have not been any significant dislocations in terms of universal service. We have also established the universal service fund to help the high cost rural areas, and together with the Congress, that will give us time to establish a separate fund, if need be, to help truly needy people who could not stay on the system.

Chairman DINGELL. Well, now, let us address this from another point. It is the Congress's policy that we shall have universal service, which means that we shall have telephones and telecommunications services as widely available as possible. Isn't this FCC decision going to cause a significant diminution of the number of telephones and of the amount of service available to large groups within our society, principally the very poor, those in rural areas?

Mr. FOWLER. We do not know that, sir.

Chairman DINGELL. Can you make a flat statement that this is not going to happen?

Mr. FOWLER. I can only say that there is a study, the Perle study, which seems to be a very good one, for 1984, which shows no effect from a $2 flat charge being imposed. That is 7 cents a day.

Chairman DINGELL. Is there any hard data in that Perle study?

Mr. FOWLER. I think there is, but I cannot speak to it. Tom?

Mr. SPIVENS. Judge Green made a mistake in basing any predictions about the impact of our access charge order on that exhibit that AT&T put into the trial record. A lot of things have happened since 1970. What the Perle study showed was——

Chairman PACKWOOD. Would you identify yourself for the record?

Mr. FOWLER. I am sorry, Mr. Chairman. This is Tom Spivens of the FCC, our Office of Plans and Policy.

Chairman PACKWOOD. Tom, what is your last name?

Mr. SPIVENS. Spivens.

Chairman PACKWOOD. Thank you.

Mr. SPIVENS. What that study showed in 1970, when the national average rate was much lower than it is today, if in 1970, local rates, which were higher than they are today, if they had then doubled, then maybe all those bad things would have happened, but we are not talking about doubling rates in 1 year from what they were in 1970.

We are looking at the benefits from other parts of cost-based competition, and a much slower rate of growth in cost, due to our phase-in. The Perle study results are just wrong, for our purpose. Perle said so himself. They are not backed up, but in a large number of econometric studies that have been done in this area there is disagreement. It is hard to predict, but the Perle study simply does not give you reliable projections for the question at hand.

Chairman DINGELL. Well, I am not sure whether you are telling me the Perle study is a good study or a bad study, whether you and Chairman Fowler are in agreement or disagreement. I gather you are telling me that the Perle study does not have hard data in it.

Mr. SPIVENS. No, sir. The original Perle study studied things on the basis of the 1970 census. Mr. Perle came back, the man who did the study, and said, you take what we did in access, which is $2, and you cannot use that study to project results from it. The author denied it and tried to go back we looked at Lester Taylor's study and a whole host of econometric studies that have been done. You do not get those dramatic falloffs from $2 a year.

Chairman DINGELL. Well, I gather that you are both praising and attacking the Perle study. I also gather that the FCC's views are at wide variance with those expressed by almost every State regulatory agency.

Let me go into just one other question here. I am continuing to exceed my time. It seems to me that your decision is a clear example of regulatory overkill. What you have done is shift all NTS costs in a single lump over a very brief period of time to end users, and have actually increased the incentive for bypass along with the cost increases that you are distributing not only to the householder but to the business users.

Mr. FOWLER. Well, I think we would disagree with that, Mr. Chairman. We do not see those two as connected. In fact, by acting as we have, we will discourage bypass, because it will make sense to continue to use our national network and get the maximum use out of it, which is not the case when you have a tremendous subsidy loaded on long distance.

Chairman PACKWOOD. Congressman Wyden.

Representative WYDEN. Thank you, Senator Packwood.

To start with, Chairman Fowler, you do not share the thesis of Chairman Dingell and myself that local rates are going to go up considerably for senior citizens and low-income persons, but I would like to ask you, is it not clear for those who are fairly well off financially, who make a comparatively large number of long-distance calls, their rates are going to go down? Would you just give me a yes-or-no answer?

Mr. FOWLER. That is true, and I guess it is also true, sir, that there are a lot of people of low-middle-income and low-income capacities who can make long-distance calls, and when they make them, they pay a subsidy to folks who may not need any subsidy at all. That is the problem with not targeting the subsidies.

Representative WYDEN. You have recommended phasing in the access charges over a transition period, and you say that that is going to avoid a substantial immediate loss of the subscriber base. Now, I see absolutely no evidence that it would not cause a longer term subscriber loss of exactly the same magnitude. What is your reaction to that?

Mr. FOWLER. Are you talking about if we progress though 1989?

Representative WYDEN. I think we are going to lose the same number of subscribers with just stretching out the period. The loss is going to be exactly the same. And I want to hear you disagree with that.

Mr. FOWLER. Well, we really do not know what will happen, what the impact will be. If we are talking here about going to a $6 flat charge by 1989, it is hard to know, but that is why we have a monitoring mechanism in effect, so that we keep and continue looking at this, together with the States, to make sure that we are still preserving universal service. Having a fund that can help folks to stay on the network is the better way to do it; target those subsidies, rather than loading a much bigger subsidy on long distance because of all the detriments to our national benefits that will accrue.

Representative WYDEN. Your access charge plan requires telephone subscribers to pay a flat fee for access to the long-distance telephone network even if they never make a long-distance call.

Now, what possible policy justification is there for requiring consumers to pay for services they do not use?

Mr. **Fowler**. The problem with that, sir, is that there is no such thing technically as saying that you are only going to have a connection for a local as opposed to long-distance when you connect into the central telephone office. I mean, there is no such thing as saying you are only connected for local service. You are able to receive long distance calls or make long distance calls with that same technical connection, because it is a switching mechanism within the central office.

So it is very difficult to say that you can only hook up the local service, because technically that is not so. But that is really a definitional thing. What we are really talking here about again is the costs of that wire from your home to the central office. Should you pay for it or not? Can you afford it? Or should you load the cost on someone else who does not have the advantages of its use when he makes a long-distance call.

Representative **Wyden**. I think that is inconsistent with everything you have been saying about cost—the theory that the customer pays only for facilities that they use. But I want to move into another area, because time is brief.

When you set up the access charge decision, did you take into effect the cumulative effect of the Bell breakup? I do not see any evidence that you did that.

Mr. **Fowler**. Yes, sir.

Representative **Wyden**. I think that is a fundamental point here.

Mr. **Fowler**. In fact, yesterday we granted a petition filed by the State of Michigan. We said that on December 1 of this year, we are going to issue a report taking into account some of these admittedly extraordinary local rate increase requests that have been filed in the States, the impact of the divestiture, and also the impact of our access charge decision, and we will issue a report at that time which obviously we would then forward to Chairman Packwood and Chairman Dingell and the Congress for its consideration, because we are concerned with universal service.

Representative **Wyden**. Let me say as my last point, to follow up on that Michigan study, I introduced, I think you are aware, with Congressman Swift a resolution requiring the FCC to do an analysis of what the breakup meant. About 160 of my House colleagues signed on in about 48 hours, and what was most interesting virtually all of them said, why in the heck didn't the FCC do that study a long time ago, before this Bell breakup came about. I would hope that you would take that back to your colleagues at the FCC. I thank the chairman.

Mr. **Fowler**. All right, sir. Thank you.

Chairman **Packwood**. Congressman Swift.

Representative **Swift**. Mr. Chairman, I was very interested in your earlier line of questioning, in which you were trying to explore where the congressional intent came from that caused this access charge decision. I thought the chairman might be interested in a conversation I had with one of the staffers who I understand was key in drafting and designing this.

I said, how come all the time we in Congress were arguing about whether we should go from SPF to SLU, and if so, where SLU should be set, we never once said we should go from SPF to zero? How did you get there? He said, oh, we, meaning the staff, never liked SLU. Some of the members of the Commission toyed with it for a while, but thank God we won. It is an anecdote that I can only verify the truth that it is an accurate statement of what was told me. I do not know what Mr. Halperin exactly meant by that.

Mr. Chairman, first of all, for the record, there have been a lot of numbers that have been thrown around here with regard to interregional revenue transfers. Would you please provide, for the record,[1] a comparison of interstate revenue flows under the current system, under various versions of the legislation that have been introduced, and under the FCC decision?

Mr. FOWLER. Yes, sir, we will.

Representative SWIFT. Thank you very much.

You keep talking about the $2 a month, and I suppose this follows up on my colleague from Oregon. What we are talking about is what the final charge is going to be. It is not going to be $2 a month when it gets ramped in. It is going to be—I hear a figure of $6 today. We have been using the $8 figure I think we got from the FCC, on a national average.

My State is already for intrastate long-distance thinking about $4, so now when you are done you have got a $12 increase in my State. That is not $2. That is not this little thing that can be easily absorbed. You are talking about very major changes when you put these things together, and that is if you go on the national average.

Now, what about those areas that are way above the national average? You do provide the universal service fund, which only clicks in when you get to a certain amount exceeding 110 or 115 percent of the national average, but then we have jacked up the national average by $8 a month.

Mr. FOWLER. Fifteen percent above the national average for rural.

Representative SWIFT. What I am saying is that I do not think that you are really presenting your case accurately when you say it is just $2 and we are going to ramp in and all of that. When you get all through, you will have increased telephone rates in the United States enormously. Will you not have?

Mr. FOWLER. Well, let me just answer that this way, sir. If we were to go through 1989—first of all, I want to say that it is premature to say that we are going to absolutely have a $6 flat rate, because we have got to make a decision in 1986, as to whether or not there has been any adverse impact on universal service to the extent that we might want to either modify the transition, lengthen the transition, or change the rates.

But assuming at that time we find that things are working pretty well, and assuming that we ultimately do go to a total of $6 in flat charges, residential customers would be paying about half of the total at that time. If you add all this up, in 1989 we estimate the charge would be $6 for the FCC flat fee and $3 for the States, if they were to go to a flat fee as well.

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[1] The information was not received at the time of going to press. If received at a later date it will be retained in the committee files.

Representative **Swift**. Mr. Chairman, what you are saying is, maybe now, if, if, if, a mountain of ifs. Maybe not. I would argue that the probability is that, yes, you are going to have a figure somewhere in the vicinity on a national average of $6. That is going to happen, and you are going to have State charges loaded on there. We are going to be following the pattern of your mechanism, which is to charge the end user rather than the long-distance carrier.

Can I just move on to one other aspect?

Mr. **Fowler**. Yes, sir. Could I just say one thing, though?

Representative **Swift**. Yes.

Mr. **Fowler**. I just think it is important when we are talking about this down the road. If you had told me in 1970 that a small Chevrolet in 1983 would cost almost $10,000, I would not have believed you. My point is that per capita and household incomes are moving up, and will, as they have in the past, so when you talk about what will be in 1989——

Representative **Swift**. Are you suggesting that access fees are going to replace normal inflation rates in telephones? No, they are going to be added to the inflation rates in telephones. You are playing with figures.

Mr. **Fowler**. No, sir. What I am saying, sir, is, if we added everything up and assume that in 1989 we had a $26 per month phone bill, and that is the total if you add all of the costs of State, local service, and the FCC flat fee, our access charge would account for only 25 percent of that figure.

Representative **Swift**. Only?

Mr. **Fowler**. Yes, sir. And the States could elect certain rate making options, such as those we talked about earlier; measured services or lifeline services. These would result in not all of the costs being shifted to flat charges to those who were truly needy.

In addition, we talked earlier about establishing a fund to be able to help poor people and others, unemployed, to stay on the system. But we think that a $13 increase spread over 6 years is not going to generate dislocations, even among the needy and the elderly. But if we are wrong, we will have in place the mechanisms to make sure that they will be able to afford that service. That is the critical point.

Representative **Swift**. How does an increase get less, simply because you spread it over time? At the end of time, it is still an increase.

Mr. **Fowler**. Yes, but each year, if you have a long transition, it means that they are not paying as much.

Representative **Swift**. It means you fool people into thinking you have not jacked their prices up by $6 or $13 or whatever it is. What you are saying is, you just want to slip them the thin edge of the wedge now, and you will shove it in later.

No further questions.

Mr. **Fowler**. That is one way to say it.

I think what we are trying to do is have smooth transition, to guard against—I was going to say any severe dislocations—to guard against rate shock.

Representative **Swift**. Maybe we should get a proctologist to help us with our terminology.

Chairman PACKWOOD. Senator Gorton.

Mr. FOWLER. I guess the point I wanted to make, sir, is that you are paying $2 a month instead of $6. That is obviously a lot less. So the transition does mean things in terms of bucks.

Senator GORTON. Mr. Chairman, I would like to follow up a line of questioning which Chairman Packwood began. Each of you agreed that the problem of more and more people going off of the system can be covered either in the kind of access charge fashion in which you did or alternatively by seeing to it that the same subsidy is paid by these new and competitive systems. But you answered his last question to the effect that the latter system which he proposes was undesirable because it would reduce innovation, it would reduce the competition of new technologies.

It seems to me bluntly, and I want your comment on this, that that is nonsense, that to say that a newer competing technology must pay the same subsidy as is now being paid or would be paid under this system by AT&T can only reduce new competition or discourage new technology if it is less efficient than the one with which it intends to compete. Is that not true?

Mr. FOWLER. What I am saying here is essentially that to the extent that for load a tax on a new technology, you may discourage it if it is only marginally less expensive to operate, for example, and the margin might be made up by that subsidy you are loading on it, and discourage it from either being introduced or employed in the first place.

Senator GORTON. So your view is that instead of subsidizing local users of the telephone service, we ought to subsidize new technology?

Mr. FOWLER. No, sir, I am not saying that. I am saying that I think that for the overall national good we need to be very careful before we start loading taxes on systems that may be more cost efficient and thereby may ultimately bring down the costs of goods and services to our American people.

We have some definitional problems, too. For example, the Wall Street Journal now transmits to remote printing plants using satellites. Is that bypass? Do we want to tax that? What about cable television? Is that bypass? Do we want to discourage that technology, or do we want to load it with costs that ultimately again are passed on to the customer?

I am not saying or suggesting that the Congress may not or would not or cannot say, yes, we are going to load those costs on there. There may be very valid policy reasons. But I am saying, I think we need to be careful about that. And again, we certainly recognize that the Congress has the final word on that, and not the FCC.

Senator GORTON. In all of your descriptions, I have not gotten an answer to this question. Is there anything which the Commission is doing at the present time to ease the upward pressure on telephone rates besides creating the universal service fund? Would you consider simply your study which is going to come out on December 1 to be a sufficient answer, or have you taken other substantive steps?

Mr. FOWLER. Well, Senator, when you talk about easing the pressures on upward rates, one that you run into immediately is inflation. Unfortunately, it is very difficult for us to have any impact. I think it is beyond our jurisdiction.

Senator GORTON. It may not affect inflation, but I am still asking the question as to whether or not you and the FCC are doing anything other than the creation of the universal service fund.

Mr. FOWLER. Yes, sir. I think we are doing several things. One, we are encouraging competitive forms of telecommunications to keep costs down, and to provide new innovation, new customer choices, better quality of services in the telecommunications area, and hopefully at lower cost. We are attempting to make sure that all the tariffs that are filed are cost justified. We are attempting to look to see whether or not we can provide more pricing flexibility in long distance services, to promote more price competition. Those are some of the things we are doing.

I hesitate to say that is the whole list, but those are some that come to mind.

Senator GORTON. And presumably you might do something else after the December 1 report, then.

Mr. FOWLER. Yes, sir. Absolutely.

Senator GORTON. Now, just a factual question. How will a change from the existing separations formula to a 25-percent across-the-board formula affect local and long-distance rates?

And a similar question. If long-distance rates are deaveraged, where will rates be above the national average, and where will they be below?

Mr. FOWLER. I will ask Carl Lawson.

Mr. LAWSON. The first part of your question, going to a uniform 25 percent, that means that the interstate share will go up in some places, and it will come down in others. And therefore presumably, depending upon what State regulators do with that, there will be some indirect effects on local rates in both directions.

Senator GORTON. Well, can you describe generically, are they likely to go up in rural areas and down in urban areas, or vice versa? And that is really the same question if long-distance rates are deaveraged. What kind of groups or in what areas are the beneficiaries of those who are penalized likely to be?

Mr. LAWSON. Probably generally the more sparsely populated places have a higher interstate allocation now, but that is not inevitably the case. The District of Columbia has a relatively high interstate allocation. Generally, the States, at least with the Bell companies, that have relatively high allocations are the mountain States in the West. Vermont, I believe, is relatively high, but there are other places. They vary all over the place. I do not recall where Washington fits. I think it is somewhere within the normal range.

Senator GORTON. Thank you for not very much.

Chairman PACKWOOD. You could supply us very specifically with those figures, could you not?

Mr. LAWSON. At least for the Bell companies.

Mr. FOWLER. Yes, we could.

Senator GORTON. I would appreciate it.

Chairman PACKWOOD. So would I.

[The following information was subsequently received for the record:]

Federal Communications Commission,
Washington, D.C., August 26, 1983.

Hon. **Bob Packwood,**
Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate, Washington, D.C.

Dear Chairman Packwood: This is in response to the questions which you and Senate Gorton raised concerning the effect of the Joint Board's proposed changes in jurisdictional separations during my testimony on July 28, 1983, at the Joint Hearing before the Senate Committee on Commerce, Science, and Transportation and the House Committee on Energy and Commerce.

As you know, the Joint Board, composed of four state and three federal commissioners, recommended that the Commission replace the present method of allocating non-traffic sensitive (NTS) local exchange costs between the state and federal jurisdictions. The NTS telephone plant between the subscriber's premises and the telephone central office is dedicated to the use of the individual subscriber and is used for both exchange and toll calling. The cost of these faacilities does not vary with the type or level of use. The present allocation of this plant is based on weighted interstate minutes of use (SPF). Under this system each telephone study area (generally a company's operations within a given state) allocates a different percentage of its NTS costs to the federal jurisdiction. This allocation has increased as a result of rising interstate usage.

The Joint Board recommends a basic 25 percent interstate allocation for NTS local exchange costs for all study areas. When combined with other measures proposed by the Joint Board, this will roughly maintain the existing nationwide division of costs between the state and federal jurisdictions. The Joint Board also recommends an additional interstate allocation for high cost areas to help keep telephone rates reasonable. This is coupled with a proposal for capping the interstate subscriber access charge to ensure that no one would have to pay more than twice the national average charge. The cost of these measures to protect subscribers in high cost areas would be paid for through carrier's carrier access charges.

To ease administrative burdens and ensure a smooth transition to the new separations methodology, the Joint Board proposes continued use of SPF (frozen at 1981 levels) during 1984 and 1985. Beginning in 1986, there would be a three-year transition for all companies from their present SPF to the new basic allocator. The additional interstate allocation for high cost areas would also be phased in over the same period. An extended transition period would be provided for areas experiencing unusually large reductions in their interstate allocations.

The changes recommended by the Joint Board would replace the untargeted support for intrastate rates produced by SPF, which has little correlation with the cost of local exchange facilities, with a system of targeted rate support for high cost areas. This will require decreases in the present level of interstate support for intrastate rates in certain areas. In general, areas with high SPFs and average or low costs will have higher intrastate revenue requirements under the Joint Board plan. Areas with low SPFs will have lower intrastate revenue requirements. Areas with average SPFs and high costs also will have lower intrastate revenue requirements. Whether areas with high SPFs and high costs will have increases or decreases in their intrastate revenue requirements depends on the relative magnitude of these factors.

Attachments A and B to this letter show the impact of the changes recommended by the Joint Board on different states. Attachment A shows that in 23 states the intrastate revenue requirement will drop. Attachment B shows that in 27 states and the District of Columbia the intrastate revenue requirement will rise because of the targeted rate support provided for by the Joint Board plan. This information is derived from a data base developed by the Commission staff which contains 1980 data for a sample of exchange telephone companies representing 98 percent of the subscriber loops in the nation. Attachment C shows the 1980 weighted average interstate SPF for each state and the new interstate allocator under the Joint Board plan. Attachment D shows the 1980 interstate SPF for each Bell System study area.

I trust that this information is responsive to the questions concerning the Joint Board plan which arose during the course of my testimony. If you have any further questions, please call Warren G. Lavey, Legal Assistant to the Chief, Common Carrier Bureau, at 632-6910.

Sincerely,

Mark S. Fowler, *Chairman.*

ATTACHMENT A.—*States* [1] *experiencing decreases in annual intrastate NTS* [2] *revenue requirements under joint board plan* [3]

State:	*Per loop*
Mississippi	$35.52
Louisiana	29.21
Alabama	24.12
West Virginia	23.93
Kentucky	21.87
South Carolina	20.48
Arkansas	19.33
Noth Dakota	16.76
Michigan	13.08
Wisconsin	10.85
Texas	9.03
Ohio	8.84
Tennessee	8.37
North Carolina	6.61
Maryland	5.27
Pennsylvania	5.05
Minnesota	3.41
Georgia	2.95
California	2.68
Indiana	2.31
Missouri	1.97
Virginia	1.73
Kansas	.37

[1] This excludes Puerto Rico and the Virgin Islands, but includes the District of Columbia.

[2] This does not include the cost of CPE, inside wire and NTS COE.

[3] These figures are based on 1980 data for a sample of telephone companies which represents approximately 98 percent of the telephone loops in the Nation.

ATTACHMENT B.—*States* [1] *Experiencing Increases in Annual Intrastate NTS* [2] *Revenue Requirements Under Joint Board Plan* [3]

State:	*Per loop*
Nevada	$49.01
Arizona	29.82
Vermont	26.87
New Hampshire	24.73
Colorado	21.50
Idaho	15.49
Wyoming	15.20
Delaware	12.89
District of Columbia	11.55
Montana	9.80
New Mexico	9.62
Nebraska	8.67
Oregon	8.43
Connecticut	7.52
New Jersey	6.99
Oklahoma	4.70
Washington	2.82
Utah	2.52
Hawaii	2.29
Florida	1.97
South Dakota	1.65
Rhode Island	1.54
New York	1.30
Massachusetts	1.00
Maine	.81
Illinois	.73
Alaska	.40
Iowa	.29

[1] This excludes Puerto Rico and the Virgin Islands, but includes the District of Columbia.

[2] This does not include the cost of CPE, inside wire and NTS COE.

[3] These figures are based on 1980 data for a sample of telephone companies which represents approximately 98 percent of the telephone loops in the Nation.

ATTACHMENT C.—STATEWIDE AVERAGE PERCENTAGE INTERSTATE ALLOCATION [1]

State	Subscriber plant factors	New [2]
Alabama	0.20474	0.32240
Alaska	.50971	.50812
Arizona	.44433	.27899
Arkansas	.26951	.35697
California	.23703	.25491
Colorado	.38259	.25585
Connecticut	.31430	.25000
Delaware	.34120	.25000
Florida	.36511	.35689
Georgia	.26222	.27802
Hawaii	.27304	.25000
Idaho	.38115	.29895
Illinois	.25656	.25019
Indiana	.23991	.25620
Iowa	.25750	.25547
Kansas	.27634	.27855
Kentucky	.19778	.30866
Louisiana	.18980	.32915
Maine	.26471	.25962
Maryland	.20750	.25000
Massachusetts	.25920	.25000
Michigan	.16733	.25480
Minnesota	.23941	.26173
Mississippi	.23189	.38038
Missouri	.26377	.27690
Montana	.38760	.33608
Nebraska	.32991	.26750
Nevada	.62463	.32231
New Hampshire	.40335	.25778
New Jersey	.30785	.25097
New Mexico	.34434	.29194
New York	.26186	.25269
North Carolina	.22041	.25978
North Dakota	.28647	.36385
Ohio	.19451	.25592
Oklahoma	.29728	.26914
Oregon	.31769	.26394
Pennsylvania	.20643	.25234
Rhode Island	.26470	.25000
South Carolina	.20871	.31239
South Dakota	.32980	.32166
Tennessee	.20148	.25099
Texas	.21422	.26446
Utah	.28062	.26266
Vermont	.44008	.30404
Virginia	.25467	.26518
Washington	.29054	.27078
West Virginia	.20791	.32367
Wisconsin	.21080	.28834
Wyoming	.51239	.45982
District of Columbia	.40630	.25000
Virgin Islands	.39440	.50174
Puerto Rico	.18801	.26296
United States	.25826	.27545

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[1] These percentages are weighted on the basis of unseparated NTS local exchange plant revenue requirements.

[2] This is the new percentage interstate allocation of NTS local exchange costs (excluding CPE, inside wire and NTS COE). This figure reflects the basic 25-percent interstate allocation for all study areas plus the additional interstate allocation for high-cost areas.

ATTACHMENT D.—*Bell System Interstate Subscriber Plant Factors (SPF)*[1]

Study area:	*Percent*
Alabama	20.01
Arizona	42.86
Arkansas	25.93
California	23.95
Colorado	39.35
Connecticut	32.30
Delaware	33.51
Florida	34.94
Georgia	26.91
Idaho:	
Mountain	34.10
PNB	37.04
Illinois	26.09
Indiana	21.84
Iowa	26.41
Kansas	27.44
Kentucky:	
South Central Bell	19.62
Cincinnati Bell	12.04
Louisiana	19.32
Maine	26.79
Maryland	21.03
Massachusetts	26.51
Michigan	16.42
Minnesota	25.18
Mississippi	23.41
Missouri	26.13
Montana	40.02
Nebraska	35.04
Nevada	60.04
New Hampshire	40.40
New Jersey	31.12
New Mexico	33.15
New York	27.10
North Carolina	22.00
North Dakota	30.08
Ohio:	
Ohio Bell	18.41
Cincinnati Bell	18.06
Oklahoma	29.82
Oregon	30.57
Pennsylvania	20.71
Rhode Island	27.34
South Carolina	20.07
South Dakota	33.01
Tennessee	20.64
Texas:	
Southwest Bell	21.35
Mountain Bell	32.48
Utah	28.52
Vermont	43.06
Virginia	25.77
Washington	28.41
West Virginia	20.63
Wisconsin	19.94
Wyoming	52.20
District of Columbia	42.18
Bell System	25.14

[1] National Association of Regulatory Utility Commissioners, 93d annual convention, at pp. 601-602 (1981).

Chairman PACKWOOD. Senator Lautenberg.

Senator LAUTENBERG. Thank you, Mr. Chairman.

Chairman Fowler, I was curious as to whether or not there has ever been a study, and perhaps you might have discussed it in response to other questions, projecting the number of those who might cancel local residential telephone service as rates rise.

Mr. Fowler. I will ask Mr. Spivins to answer that, Senator.

Senator Lautenberg. I assume the answer will be the same, no matter whom it comes from.

Mr. Fowler. Not necessarily. That is why I thought I would ask him.

Mr. Spivins. As local rates go up, exactly who and what would cancel——

Chairman Packwood. Would you speak a little more into that microphone? I cannot hear you.

Mr. Spivins. The loss from cancellations as local rates go up will depend in part on what series of options States and the Federal Government jointly adopt to keep the basic lifeline rates down. It will also depend upon how much consumers value the additional choices they are given both in long distance and in terminal equipment. There are studies, but they are both broad brush studies, and they indicate that even if States do not adopt local measured service options, and even if consumers do not place very much value in buying their own phones, and even if a lot of other bad things happen, we will still have very high rates, very high rates of penetration. All studies are imperfect, but the consensus of them seems to be that a high level availability of service will be maintained, given the type of service ranges we are talking about, in the 90 percent in terms of households, above the 91 level which is Judge Green's benchmark. Exactly how much will depend on these other options?

Senator Lautenberg. It is a more complicated answer than my question asked for. I appreciate the effort, but when we start talking about options and things of that nature, we are getting away from the point. I am talking about how to insure that we keep that instrument in the house, so that the individual can communicate on it as needed on an emergency basis. I am discussing simply keeping that phone line in there.

Now, we have had some figures presented to us that suggest that for every 10-percent increase in local costs, you might lose as much as 1 percent of your subscribers in a State like mine, a densely populated area. That would be very significant and very painful for those people who might lose that service. And of course, the result is, you have fewer people covering the total cost configuration, and the burden just keeps getting worse.

Mr. Chairman, I would appreciate it if you or your staff people could review the bill I have introduced. Based on the enthusiasm with which you have greeted others, perhaps I should be pleased that you have not reviewed mine yet, but I would appreciate it if you would review it and pass back any comments to us in writing. My approach is to target support for those individuals who are needy as opposed to running the risk of rewarding inefficient, high-cost systems. I fear that even the joint board's plan runs that risk, by subsidizing most of a system's costs that are more than 15 percent above the national average. In fact we should not be satisfied with just average performance. We should be striving to get costs down further.

Am I correct that the joint board's universal service plan would run somewhere around $400 million?

Mr. FOWLER. It is about $565 million in 1984, sir.

Senator LAUTENBERG. In 1984. OK. Have you projected its growth beyond 1984?

Mr. FOWLER. Yes, indeed. It is funded every year.

Senator LAUTENBERG. So you have projected its growth beyond 1984?

Mr. FOWLER. I do not think we have, but I think the mechanism is such that it is designed to take care of those costs.

Senator LAUTENBERG. Mr. Chairman, one quick question, which I hope will get a quick response.

Chairman PACKWOOD. Go ahead.

Senator LAUTENBERG. Do you think that if the carrier is held harmless for a large part of his costs that are 15 percent above the national average, there will still be an incentive to make these systems more efficient, to drive the cost down. What is your view on that?

Mr. FOWLER. Our view is that we think the 15-percent margin is a significant enough margin to provide the incentives to be efficient and to build efficient systems, and of course we would hope that the States would help us in policing those costs to make sure we do not have gold-plated systems or inefficient systems. Beyond that, we are willing to take some risk for the societal good at large, to make sure that our people in rural areas can still have their telephone service by implementing that subsidy but it is not a perfect mechanism. But we think on balance it is a pretty good one.

Senator LAUTENBERG. Thank you, Mr. Chairman.

Chairman PACKWOOD. Frank, I have heard that statement used a time or two before. For each 10-percent increase, a 1-percent drop in customers. And that was in your maiden speech. Is that from your Public Service Commission, or what is the source of that? I am advised that is the Perle study. Is that correct?

Senator LAUTENBERG. Yes.

Chairman PACKWOOD. Thank you.

Senator Ford.

Senator FORD. Thank you, Mr. Chairman.

I appreciate all the studies and references, and they are not all correct, and that sort of thing.

Mr. Chairman, may I ask you a question?

Chairman PACKWOOD. Yes.

Senator FORD. Did I understand you a moment ago to direct to Mr. Fowler this question, that rates will not be changed because of the AT&T breakup?

Chairman PACKWOOD. The long-distance rates. I asked him if the FCC fixes long-distance rates? The answer is yes. Is there anything in the divestiture decree that in any way affects their rights to set long-distance rates where they want them? No, it does not.

Senator FORD. That is the way I understood it, Mr. Chairman. I thank you for your courtesy.

Congressman Oxley made a statement a few minutes ago that his information was from some people that made some studies that apparently had been made available to him that the rates would double in the next decade. You stated a moment ago that long-distance rates would come down 35 percent, I think over the next 10 years, the next decade.

Mr. **Fowler**. We expect by 1984.

Senator **Ford**. But you are adding $6 to the access charge, so whatever break they get will be taken up by the access charge.

Mr. **Fowler**. But if they make six or more average long-distance calls, they will actually be better off, Senator, with the reductions.

Senator **Ford**. I understand that, but if I do not make them, I am worse off.

Mr. **Fowler**. Yes, sir.

Senator **Ford**. So you can have it either way you want it, Mr. Fowler, either way you want it, and you can always make the sheets come out or the studies come out, or you can reflect on their accuracy or their authenticity. You know, you can do all of those things. I am not a word merchant, and I do not understand all the facts and figures. If my bank book balances at the end of the month, I feel like I am lucky. You may be talking about rates dropping but they are going up.

As of last night on the national news, there is $4 billion in new telephone rate increases before the various commissions around this country. Is that correct?

Mr. **Fowler**. I do not know if that is the exact figure, but it sounds like it might be.

Senator **Ford**. It sounds good, does it not?

Mr. **Fowler**. No, it does not sound good.

Senator **Ford**. Oh, it does not sound good?

Mr. **Fowler**. I am sorry.

Senator **Ford**. But all of them are based on the breakup. Come January 1, 1984, the various companies are now going to have to pay their own way. So we have got $4 billion facing us today.

I do not know where the decade came from, or the 10 years, but in my State we are having rate increases filed that will immediately double the rates. Now, do you have many States—I think Texas was triple, if I am not mistaken—facing a situation like this?

Mr. **Fowler**. I alluded to that in my testimony, Senator, and I think it is useful to focus on one fact. Roughly, since 1970—there was a study done of all the rate requests made in the States——

Senator **Ford**. Here we go with another study.

Mr. **Fowler**. This one is pretty accurate.

Senator **Ford**. Is that the Perle study that he referred to that was no good?

Mr. **Fowler**. No, sir.

Senator **Ford**. OK.

Mr. **Fowler**. It showed that 93 percent of the requests were not granted at the level of the request. They were significantly reduced. So I think it is significant to remember that they start off asking for a lot. They may not get that much from the States. These are rate requests that are pending.

Senator **Ford**. Do you know what pancaking is in a rate request?

Mr. **Fowler**. No, sir, but I think I am about to.

Senator **Ford**. You put in for a rate increase, and while they are deciding on that one you put another one right on top of it. And you keep right on going, and you pancake.

Let me ask you this question before the little red light comes.

What do you think the rates will be 10 years from now, including the inflationary costs and all the other things that are going to be added on? What is your estimate of the urban and rural cost of telephones 10 years from now, residential?

Mr. **Fowler**. I cannot adjust it for inflation, Senator, because I do not know if I can predict that.

Senator **Ford**. Well, try. You have had a lot of studies. You can take one or the other.

Mr. **Fowler**. Well, whatever that is, I cannot tell you. I can tell you what it would be without the inflation. We think it would be at the end of 1989 about $26 a month, and remember, that is 6 years from now, but it does not necessarily phase in until we make certain decisions along the way. At that time, as I said before, long distance would be about 35 to 40 percent less.

Remember, that is the cost of the wires from the homes to the office.

Senator **Ford**. I have heard more about wires this morning. The phase in from the home to the building. That is fine. We are going to pay for those. But you can also send your phone back to the telephone company and buy one for $9.88 downtown. It has even got a little number you punch that will redial the last number. So you do not have to pay the telephone company. That would reduce your monthly charge. And they are getting out of that business, and I certainly do not blame them. They have got all the money now, and the phone is worn out.

Mr. **Fowler**. Senator, that is a very good point, because in the past you had to rent your phone from the phone company for $35 a month, and with——

Senator **Ford**. $35 a month?

Mr. **Fowler**. $35 a year. I am sorry.

Senator **Ford**. The service is cheap. The phone is expensive.

Mr. **Fowler**. $35 a year, and now, as you indicated, you can go to an A&P food store and buy a phone for $9.95, or buy one for $15.95. So that is something that is going to bring the overall cost down. Before, that was buried in your bill, and you are right.

Senator **Ford**. Oh, we are not going to bury anything. Everything is going to be resurrected, isn't it, Mr. Chairman? May I ask one more?

Chairman **Packwood**. Go ahead.

Senator **Ford**. Since we have talked about the study, and you are going to have one due in December, is there any way you could accelerate that study, so that we might use it in trying to make decisions as it relates to this legislation?

Mr. **Fowler**. It is going to be very difficult, Senator. We granted just yesterday a petition from the State of Michigan. The States are going to come in in September. They need some leadtime to get all of the information. Then we are going to study all of that and try to come up with a report on December 1, and we are on a very fast track. So it would be very difficult for me to promise anything better than that, I am afraid.

Senator Ford. We can ask the General Accounting Office to do it also.

Chairman Packwood. We can ask them. I do not know if they will do it any faster, but we can ask. We are aiming for a markup in September.

Senator Ford. I understand that. But this is pretty emotional, and we need all the answers we can get.

Representative Wyden. Mr. Chairman.

Chairman Packwood. Who is calling?

Representative Wyden. The gentleman from Oregon.

Chairman Packwood. Yes, Ron.

Representative Wyden. Would the gentleman from Kentucky yield for just one quick question?

Senator Ford. The red light is on. If you can get past it, that is fine.

Representative Wyden. I would ask my chairman, an Oregonian, if I could have unanimous consent to ask a question.

Chairman Packwood. Go right ahead.

Representative Wyden. Mr. Fowler, why was that study not done before the original access charge came down? Why didn't the FCC go out and take a look at what this was going to do to our elderly, rural, and low-income people? I have never heard why you didn't do this a long time ago, why you are doing it now. Is it because of the resolution with 160 sponsors, and because of all of the pressure? I think it would be helpful to us to know why you did not do it a long time ago.

Mr. Fowler. I think the answer, Mr. Wyden, is that first of all we requested a great deal of information from the States on this, and we heard a lot of anecdotal evidence of what would happen or not happen, but there have been very few studies, surprisingly, conducted anywhere. We felt that looking at an initial $2 per month increase, that we did not think there would be any significant problem, and that is the reason why we now have set up this monitoring system, to make sure that as we phase this in—and particularly I am talking about 1986—that it will not have any precipitous or undue impact upon universal service.

Representative Wyden. I thank the chairman. I am glad you admitted you were wrong.

Mr. Fowler. Well, if I have, it will not be the first time.

Chairman Packwood. Senator Danforth.

Senator Danforth. Mr. Chairman, I would like you to look down the road 3 years, in percentages, and give me some idea as to what the residential telephone user would see in changes in his phone bill over the next 3 years for residential service.

Mr. Fowler. I guess that would be 1986. We would be looking at a $4 flat charge per month as a result of our access charge decision. The standard estimate from State increases would be roughly $2 more, so assuming that we are now about $11—about $18, Senator.

Senator Danforth. I do not want dollars. I would like percentages, if I can get that.

Mr. Fowler. We could calculate that, sir.

Senator Danforth. Let me just ask you this. I want public service increases, whatever you think people are going to have. If somebody looks at his residential bill right now, Joe Dokes opens the mail and gets the phone bill, and he sees an amount. Let us call that x. Looking down the road 3 years, will it be x, 2x, 3x? What will it be?

Mr. **Fowler**. Well, we can give you some numbers as to what an average would be and the percentage increase, and we can work that out, Senator.

Senator **Danforth**. What is your best guess?

Mr. **Fowler**. I just cannot give you a percentage right now.

Senator **Danforth**. Do you have any range that you could give us? I am sure it will differ from State to State. Do you have just a general idea of what we are looking at?

Mr. **Fowler**. The reason I shy away from percentages is, you have to say compared to what, and in some States, there are local flat charges, for example, that have been held down artificially to as little as $5 a month or $6 a month. So for each State, that number is going to be different when you try to calculate the Federal and State charges together, so it is hard for me right off the top of my head to give you those kinds of numbers, but I would be glad to.

Senator **Danforth**. Well, in Texas, they have asked for what? What was the increase that Southwestern Bell asked for in Texas?

Mr. **Fowler**. That is with the Texas Public Utility Commission. They have asked to go from $10 basic rate to $30.35 a month, and that is one, of course——

Senator **Danforth**. That is more than threefold. That is just for the basic rate. And then there is the access charge on top of that.

Mr. **Fowler**. I said in my testimony there is a great deal of question surrounding that kind of rate increase. We are talking here for our part of adding $2 a month. This rate, rate increase here cannot be—although they have attempted to say it is—because of our access charge decision. That is not correct.

Senator **Danforth**. That is my second question. I really have two questions. One is, what are people going to be looking at? I am talking about the average telephone user—residential. What is that individual going to be looking at over the next 3 years in percentage increase? Whatever the phone bill is now, what will it be in 3 years? Will it be the same? Twice as much? Three times as much? Four times as much?

Mr. **Fowler**. It is difficult to answer that again, because with the shifting to flat charges, but long distance coming down on a given individual's bill, it will depend upon his telephone usage habits.

Senator **Danforth**. I am talking only about residential—local, just the local. Somebody who never makes a long-distance call.

Senator Ford: You still get charged.

Senator **Danforth**. What would it be? Would you know?

Mr. **Fowler**. It would probably double.

Senator **Danforth**. Probably double in 3 years?

Mr. **Fowler**. Yes, sir.

Senator **Danforth**. It could be more than that, right?

Mr. **Fowler**. No, we do not think so, but I mean that is our best estimate.

Senator **Danforth**. OK. Now, of that doubling, of that 100-percent increase over 3 years possible, could you break that down into its component parts? Could you tell us, if you would consider that increase as a pie, how much of that would be caused by the access charge?

Mr. **Fowler**. $4.

Senator **Danforth**. Again, please not dollars. It is really apples and oranges. Let us take the percentage—100 percent is a pie.

Mr. **Fowler**. We can figure this out, and I will ask Tom to do that now. I will give it to you in a moment. It is about half.

Senator **Danforth**. About half of it would be access charges? And what would be the other half of the pie? Part of it would be inflation, would it not? General inflation would be part of it? What else? Depreciation would be part of it? What else?

Mr. **Spivins**. Generally, the BOC's current rates of return are below what they are allowed.

Senator **Danforth**. And part of it would be that the business rates would tend to be held lower than this correctly indicates. Would that be correct?

Mr. **Fowler**. The flat charge would be up. It would be $6. But long distance would be down. Again, you are talking about local service only. It follows the same proportions, in any event.

Senator **Danforth**. In any event, if the access problem were solved, that is, if there was no increase in the access charges for residential users, that would reduce the rate increase by half, right?

Mr. **Fowler**. I guess that is right. Yes, that is right.

Senator **Danforth**. Thank you.

Chairman **Packwood**. Congressman Wirth, I do not think you got in on this round.

Representative **Wirth**. Thank you, Mr. Chairman.

Let me make a couple of points, and then go back to Senator Danforth's question, so that we all understand what it is we are talking about here.

First of all, Chairman Fowler, we have all debated this access charge issue off and on for a long time. It is a balance, as we have said so many times, between economic efficiency on the one hand and social policy on the other. We worked with you all last December on the access charge question, and our subcommittee disagrees with you all with where that balance is.

We are not going to solve that problem here, but let us all be aware of the fact that that is the balance, that where we do disagree we think greater weight ought to be placed on social policy, the universal service question, and you think there ought to be greater weight on economic efficiency, and that is legitimate.

Mr. **Fowler**. I do not agree with that, sir.

Representative **Wirth**. You do not agree with that statement?

Mr. **Fowler**. No, sir, because we do believe that universal service is one of the touchstones.

Representative **Wirth**. I know you do, but it is where you put certain weight. We would tend to put more weight one place than you would.

Mr. **Fowler**. No, I do not agree with that.

Representative **Wirth**. Now, on the economic efficiency question, where you put the greater emphasis, it seems to me that you also miss a significant point, and that is that one major contributor to economic efficiency is universal service. The fact that 91 percent, and hopefully 100 percent of households would have a telephone contributes, it is difficult to measure directly in the fashion that you all are looking at rates, but that universal service does contribute to the economic well-being of this society, as you pointed out in your testimony, tying everybody together. But beyond that, making sure that people can call a Sears and Roebuck, or that there are economic benefits, that Citibank is in touch, can be in touch with all of the consumers in New York City, for example.

There are economic values in universal service which I think you ought to factor in more thoroughly in your analysis, but leaving that aside, we have discussed that, and disagree on those arguments.

Let me go back, if I might, to a very important question raised by Senator Danforth, which was also touched by Congressman Swift in his questioning. What we have to do is make very sure and clear here that even if the Packwood bill or the Wirth, Dingell, and so on bill passes, that is not going to solve all of these problems. There are two other major legs to the stool. One of those legs relates to what the Bell operating companies are able to get out of the State public utility commission in terms of rate requests and what they justify.

We do not have any control over that. That is up to the State PUC's, and that is the next panel. You would agree with that, that that is a second major influence? You cannot say that what we are going to do is increase or decrease telephone rates by a certain percentage, as you pointed out, Mark, because there is that unknown factor of what each State PUC does. We do not have any control over that.

Mr. FOWLER. Right.

Representative WIRTH. The second major factor that we do not have any control over is what happens between the local operating company and the parent in terms of the allocation. If the local operating company does not get its fair share of the assets, then they are going to have to raise their rates in order to continue to serve that area.

If they get less valuable assets, their rate of return has to go up to be able to provide universal service to that area. That is the second major piece, again, that we do not have any control over.

We have control over about a third of what goes on. Let us remember that, and not assume that what we are going to do in this legislation is going to solve all those rate problems, because it is not going to do it.

The point that Mr. Swift makes is very important. The precedent that we set, the example that we set, is terribly important. The State PUC's are not as well staffed as you are, and State public utility commissioners I do not think maybe have available all of the expertise that we may have available, and they are going to be looking at what we do, which is the point that Congressman Swift made.

That is why this legislation is so terribly important in the impact that this is going to have on State PUC's, and we would hope also the message that we send to the local operating companies that they have got to get their fair share, which is why we argued last year over asset evaluation before divestiture. We thought that that was a good idea, to get the State PUC's to be making those decisions, and the local operating companies.

But again, I just wanted to go back to Mr. Swift's point that it is terribly important, the precedent and example that we set in this legislation is very significant, and we ought to do that sooner rather than later, which is why I think we all hope this legislation will get through early this fall.

Mr. Chairman, thank you very much. It is really not a question, but rather to try to put this in the appropriate context, I think, and help Mark in not being able to answer the specifics of that question. You cannot do it.

Chairman PACKWOOD. I think you did a very good job of it.

Congresseman Lent has not asked yet.

Representative LENT. Thank you, Mr. Chairman.

Chairman Fowler, you have been put through the grill a little bit this morning by different Representatives concerning the problems of the poor and why did the FCC not look at the poor and the indigent and the elderly in connection with constructing this FCC proposal providing access fees. I hope that you would give an answer that I am going to suggest to you, which is that my understanding is that any company, any one of these regional companies can go to the State and suggest a system such as a lifeline rate, which has been talked about a little bit here this morning.

I know that the regional company that will service the area that I represent in New York is going to propose a lifeline rate of $5 a month for a zero allowance measured service. No customer access line charge would apply, assuming the FCC grants a waiver that will be requested by the State or utility.

Is that a workable way of getting around this problem? Perhaps it is even a red herring problem, of the poor and the elderly that has been raised this morning?

Mr. FOWLER. Well, sir, we specifically in our order made that accommodation that you spoke of that provides for waivers of our flat charge in order to permit somebody to take lifeline service. In this case, you are talking about the State of New York and a $5 per month lifeline service. That is something that we anticipated and indeed built into that order. So, yes, we do have that additional safety valve there.

In addition to that, we also have said that by providing a very long transition period here, it will give Congress time to fashion any additional remedy. That is an external targeted subsidy fund to help people who might not even, for example, be able to afford that lifeline service.

Representative LENT. So that all of this concern that we have heard this morning about access charges being imposed on the poor and elderly, there is no need for that, if the local State and local regional utility applies for a waiver for a lifeline type rate. It may vary from one region to another, but it is perfectly permissible and the attitude of the FTC would be to grant a waiver, assuming it is a reasonable application.

Mr. FOWLER. Yes, sir.

Representative LENT. As opposed to the bills that we have been talking about that have been introduced would do, which would be to continue a subsidy for everyone. The rich rancher out in Wyoming or Montana and the wealthy widow who lives in Grosse Point, they would—under the terms of this bill there would be a continuing subsidy for those people.

Mr. FOWLER. That is correct.

Representative LENT. Now, one other thing. All of the recent legislative proposals, as I understand it, would scrap this access plan that took the FCC and the entire industry over 5 years to develop, and in its place these legislative proposals would require that all of the costs for access for long-distance service be recovered from the long-distance carriers.

These bills go on and recognize that there is going to be a tremendous incentive for bypassing the existing system in one way or another if they attempt to recover from these bypass operations by either a tax or a fine.

From your point of view as an expert in this field, is it not questionable whether that kind of a plan could work, since in most cases these bypass operations would be set up in an effort to avoid the higher charges for long-distance lines?

Mr. FOWLER. Sir, you raise a very good question. That is a difficulty. First, there are definitional problems and I touched on those earlier: Where do you draw the line? Is it bypass when the Wall Street Journal uses satellites to print its daily edition by transmitting the information by satellite to its regional printing presses. Is cable television bypass?

Representative LENT. Also, is there not a problem with enforcement?

Mr. FOWLER. It is very difficult to detect.

Representative LENT. Under the terms of the Packwood bill, with its concept of fraudulent bypass, you almost have to get inside the customer's head. If a customer is buying a particular circuit to avoid access charges, that is illegal and the fine applies. But if he gets in to buy a circuit to buy some new feature or to provide quicker operation or for some other reason, then that is legal.

Who is going to police this? Is it the local telephone company, is it the bypass company, is it the FCC, is it the district attorney? Is this really a workable system?

Mr. FOWLER. It would certainly present, sir, some very grave enforcement problems. Again, I would say that we share the concern of all of these difference pieces of legislation and the only question is what is the best way to do it. I mean, we are all on the same sheet of music in terms of what our concerns are.

Representative LENT. Thank you, Mr. Chairman.

Chairman PACKWOOD. Let me again indicate to the committees, we have got three panels to go. It is our intention to go right through, although we would take about a 5-minute break, 5 or 10 minutes, when we are done with Chairman Fowler.

And I think Senator Riegle has not had a chance to ask on this round.

Senator RIEGLE. Thank you, Mr. Chairman.

The Michigan Public Service Commission has stated that a customer who currently secures single party line, unlimited local telephone service from Michigan Bell at a rate of $10.17 a month, will be faced with a bill of $20.95 per month for the same service during 1984.

Now, that is their official and public assessment. That is more than a doubling of rates within a period of a year's time. Now, is that accurate in your view, and what is your reaction?

Mr. **Fowler**. I do not know if it is or not. It may well be, sir, and I have no reason to question that figure. But I would emphasize that our access charge decision can only load $2 on to the bill in 1984.

Senator **Riegle**. Have you done a State-by-State analysis as to what basic telephone service costs today and what it is going to cost within 1 year's time.

Mr. **Fowler**. The answer is that we are doing that, in response to a petition that was filed by the State of Michigan.

Senator **Riegle**. And if I heard you right earlier you said you were going to have the results later in the year.

Mr. **Fowler**. December 1, sir.

Senator **Riegle**. I do not think that is sufficient. Let me tell you why. And I want to appeal to the chairman if I can on this.

You know, you can spend as long as you want doing a study and the quality to some extent will vary with the time afforded. However, I do not think we can wait until December 1 for that kind of an assessment. I think we need a 30-day or a 45-day study.

In other words, I think the FCC has to go out and do this job fast, and I think you have got to get back in here with the results as best you can determine. We have got to be in a position to write law and we have got to be in a position to write a law this year.

Chairman **Dingell**. Would you yield, Senator? Would you yield to that?

Senator **Riegle**. Yes, I would.

Chairman **Dingell**. We have a survey which our committee has had its staff make of all of the State regulatory agencies and the impact of the FCC's actions on phone rates. It has been carefully prepared on the basis of a telephone survey of the State agencies I think that it would be helpful, and I ask unanimous consent that the survey be put into the record at this point.

Chairman **Packwood**. That will be done.

[The material referred to follows:]

SURVEY OF LOCAL TELEPHONE RATE INCREASES FILED WITH STATE PUBLIC UTILITY COMMISSIONS

The following survey of local telephone rate increases in all 50 states and the District of Columbia has been compiled by the staff of the Committee on Energy and Commerce. This survey was compiled in July, 1983. Public utility commissioners were contacted and asked to provide an overview of recently granted, pending and anticipated requests made by telephone companies in each jurisdiction for increases in basic monthly subscriber rates. The state commissions were asked to identify the amount of such requests, their contributing factors and their impacts on local customers.

Complete information in each state is not available due to the nature of filing practices which vary from jurisdiction to jurisdiction. For instance, certain states require historical test years while others permit projected test years. Thus, where a historical test year is used, the impacts of the FCC access charge and depreciation decisions, the divestiture and other recent developments by law cannot be factored into rate designs until they have been in effect for at least one year.

Nevertheless, the survey demonstrates a pattern of local rate increases awarded and requested significantly in excess of the historical norm. There are 26 pending rate increase requests totaling approximately $7.0 billion. All but two of the increases relate in part to FCC decisions and the divestiture. The full consequences of these rate increases and requests cannot be precisely ascertained at this time, but in a number of states they would result in at least a doubling of basic monthly customer charges. The accompanying chart depicts the status of filings in each state by major component.

ALABAMA

South Central Bell was granted a $117 million rate increase which took effect 1/11/83. This increase is attributed to the FCC depreciation decision and to normal increases in operating costs. The full increase would affect residential and business customers equally. The PSC expects South Central to file another rate increase request after 1/1/84. That increase is expected to incorporate the effects of the FCC access charge decision, the divestiture, the deregulation of CPE, and the loss of intrastate toll revenues.

ALASKA

Alascom has no rate increase requests on file at the present time.

ARIZONA

Mountain States Bell has a $79 million rate increase pending. The case was filed on February 21, 1983. This increase is attributed to a loss of revenues due to long distance competition and normal increases in operating costs. The full increase would raise basic service rates by over 100%, with average residential rates going up by 67%. These rate request incorporates an 8% drop in intrastate toll rates. The PUC could not predict what Mountain States will ultimately be granted.

ARKANSAS

Southwestern Bell has a $138 million rate increase pending. The case was filed on March 23, 1983. The increase is attributed to the FCC access charge decision, the FCC depreciation decision ($69 million of the increase), the deregulation of CPE and new state access charges. The full increase would affect residential and business access line charges equally. The PSC historically awards between 2/3 and 3/4 of Southwestern's rate requests.

CALIFORNIA

Pacific Telephone has an $838 million rate increase pending. The case was filed in January, 1983. The increase can be attributed to normal increases in operating costs. On July 5, 1983, Pacific ammended its filing by requesting an additional $500 million to incorporate the effects of the FCC depreciation decision and the divestiture. An additional $745 million has also been requested to incorporate the FCC access charge decision. The full increase would raise average residential flat rate service from $7.00 per month to $18.35 per month, a 162% increase. Business rates would rise from $14.55 to $27.25 per month, a 87% increase. To date, the PUC has recommended that Pacific receive $297 million of its $838 million request. Residential customers are expected to be hurt the most by the rate increase.

COLORADO

Mountain States Bell was granted a $38 million rate increase in May, 1983. It had requested $105 million. This increase is attributed to the FCC depreciation decision and to Computer II. The full increase would affect residential and business customers equally. The PUC expects Mountain States to file another rate increase request around 1/1/84. That increase is expected to incorporate the effects of the divestiture.

CONNECTICUT

Southern New England Telephone was granted an $89,024,000 increase which took effect 11/24/82. It had requested $127.9 million. This increase is attributed to normal increases in operating costs. The PUCA expects Southern New England to file another rate increase request after 1/1/84. That increase is expected to incorporate the effects of the divestiture.

DELAWARE

Diamond State Bell Telephone has a $25.9 million rate increase pending. The case was filed on June 1, 1983. The increase is attributed to the FCC access charge and depreciation decisions, and to the divestiture. The access charge decision alone would mean a $2.00 and $4.00 increase in per line residential and business rates respectively.

DISTRICT OF COLUMBIA

The Chesapeake and Potomac Telephone Company has an $82 million rate increase pending. The case was filed on March 15, 1983. The increase is attributed to the FCC depreciation decision, the deregulation of CPE and the loss of PBX's. C&P has proposed raising residential rates by $39 million, business rates by $33 million and government rates by $8.6 million. C&P has requested that $26 million of the request be granted immediately to preserve its AAA bond rating.

FLORIDA

Southern Bell was granted a $113 million rate increase which took effect on June 22, 1983. It had requested $404 million. The increase is attributed to normal increases in operating costs. The PSC could not predict whether Southern Bell would re-file after 1/1/84.

GEORGIA

Southern Bell has a $158,463,000 rate increase pending. The case was filed on March 2, 1983. This increase is attributed to the FCC depreciation decision, the deregulation of CPE and normal increases in operating costs. The full increase would raise residential rates from an average of $7.35 per month to $11.55 per month, a 57% increase. Business rates would increase from $15.50 per month to $21.80 per month, a 41% increase.

HAWAII

The Hawaiian Telephone Company has an $82,368,000 million rate increase pending. The case was filed on December 30, 1983. The increase is attributed to the FCC depreciation decision and the deregulation of CPE. On the island of Oahu, the full increase would raise residential rates from $10.90 to $19.00, a 74% increase and business rates from $29.85 to $45.50 a 52% increase. A ruling is expected in early 1984.

IDAHO

Mountain States Bell has a $34 million increase pending. The case was filed on December 20, 1982. This increase is attributed to normal increases in operating costs. The full increase would raise basic exchange service rates by 80 to 120 percent and business rates by 50 to 75 percent. Intrastate toll rates would decrease by 10 to 12 percent. The PUC has recommended an intrastate toll increase and a 10% rise in basic exchange service rates. The PUC expects Mountain States to file another rate increase request at the conclusion of the current case. That increase is expected to incorporate the effects the the FCC depreciation decision.

ILLINOIS

Illinois Bell was granted a $21 million rate increase in February, 1983. The increase is attributed to normal increases in operating costs.

INDIANA

Indiana Bell Telephone has a $96 million rate increase pending. The case was filed in May, 1983. The increase is attributed to the FCC access charge decision, the deregulation of CPE, and to the divestiture. The PSC believes that residential customers will feel the greatest impact of the increase.

IOWA

Northwestern Bell has a $49.7 million rate increase and a $19.1 million rate increase pending. The first case is attributed to normal increases in operating costs and the second case is attributed to the deregulation of CPE and inside wiring in Iowa. The full increase would raise residential and business telephone rates equally in the first case. The ISCC has commented that it would not be receptive to a post-divestiture rate increase.

KANSAS

Southwestern Bell has a $213 million rate increase pending. The case was filed on May 5, 1983. The increase is attributed to normal increases in operating costs and to a Kansas access charge decision. The full increase would raise local exchange rates $110.5 million and intrastate toll rates $11.4 million. The KSCC should rule on this request by the end of the year.

KENTUCKY

South Central Bell filed an intent to increse telephone rates. South Central is expected to file its request by July 29, 1983.

LOUISIANA

South Central Bell was denied a $238 million rate increase request on May 19, 1983. South Central appealed the decision to US District Court, which ordered the PSC to grant South Central an increase commensurate with the higher costs the company will face due to the FCC access charge and depreciation decisions. After the PSC awards that amount, South Central is expected to appeal to the Louisiana Judicial Court to get the remainder of the $238 million.

MAINE

New England Telephone and Telegraph was granted a $11.4 million rate increase. It had requested $49.8 million. The PUC expects New England to file another rate increase request in the fall of 1983. That increase is expected to incorporate the effects of the divestiture.

MARYLAND

Chesapeake and Potomac has a $218 million rate increase pending. The case was filed on June 3, 1983. The increase is attributed to the FCC access charge decision, the deregulaticn of CPE, the divestiture and increased competition in the long distance market. The full increase would raise residential rates by $156 million or 36.9%. Business rates would rise by 10.3%. Intrastate long distance rates would decrease by 3.3%. The PSC will rule on the request by December, 1983.

MASSACHUSETTS

New England Telephone is expected to propose a rate increase which would incorporate the FCC access charge decision sometime in the future.

MINNESOTA

Northwestern Bell Telephone is expected to propose a rate increase in excess of $100 million around September 1, 1983. Northwestern was granted a $56 million increase in April, 1983 which raised residential and business rates by 24%.

MICHIGAN

Michigan Bell has a $450 million rate increase pending. The case was filed in November, 1982. The increase is attributed to the FCC depreciation decision and the deregulation of CPE. The PSC expects to grant $182 million of Michigan Bell's request. This amount would increase residential rates by $3.00 per month and business rates by $5.00 per month. Michigan Bell has also requested an additonal $100 million due to the FCC access charge decision.

MISSISSIPPI

South Central Bell was denied a $98 million rate increase. South Central has appealed this ruling. The PSC expects South Central to file another rate increase request in September, 1983. This filing is expected to incorporate the effects of the FCC access charge and depreciation decisions.

MISSOURI

Southwestern Bell Telephone has a $254 million rate increase pending. The case was filed on February 1, 1983. The increase is attributed to the FCC access charge and depreciation decisions, the deregulation of CPE and to the divestiture. The full increase would raise average residential rates from $7.65 to $17.10 per month, a 124% increase. Average business rates would rise from $20.13 to $42.66, a 112% increase.

MONTANA

Mountain States Bell has a $20,710,000 increase pending. The case was filed in March, 1983. The increase can be attributed to the FCC access charge decision, the deregulation of CPE and normal increases in operating costs. The full increase would raise average residential rates from $6.78 per month to $7.64 per month, a 13% increase and raise average business rates from $17.64 to $19.88, also a 13% increase.

NEBRASKA

Northwestern Bell was granted an $8,033,000 increase January 11, 1983. It had requested $42,700,000. The increase is attributed to the FCC depreciation decision. The PSC expects

Northwestern Bell to file another rate increase request shortly. That increase is expected to incorporate the effects of the FCC access charge decision, the deregulation of CPE and the divestiture.

NEVADA

Nevada Bell was granted a $5,857,000 increase on June 27, 1983. It had requested $17.4 million. The increase is attributed to normal increases in operating costs. A prior increase incorporated the effects of the deregulation of CPE. The PSC expects Nevada to file another rate increase request around 1/1/84. That increase is expected to incorporate the effects of the FCC access charge decision and the divestiture.

NEW HAMPSHIRE

New England Telephone and Telegraph was granted an $8,380,000 rate increase which took effect on July 17, 1982. The increase is attributed to normal increases in operating costs. Local exchange service rates rose by 7 1/2% overall. The PUC expects New England Telephone to file another rate increase request after 1/1/84. That increase is expected to incorporate the effects of the FCC access charge decision and the divestiture.

NEW JERSEY

New Jersey Bell has a $245 million increase pending. The case was filed on November 18, 1982. In May, 1983, $29 million of that filing had been acted upon. The increase is attributed to the FCC depreciation decision and to normal increases in operating costs. New Jersey Bell has proposed that $157 million of the increase be paid by basic exchange customers. The BPU expects New Jersey Bell to file another rate increase. That increase is expected to incorporate the effects of the divestiture.

NEW MEXICO

Mountain States Bell has a $86.1 million rate increase pending. The case was filed on June 17, 1983. The increase is attributed to the FCC access charge and depreciation decisions, the deregulation of CPE, the divestiture and Computer II. The full increase would raise residential flat rate service from an average of $9.91 to $27.92, a 182% increase and raise business service from an average of $28.91 to $55.83, a 93% increase.

NEW YORK

New York Telephone is expected to file a rate increase request in excess of $1.00 billion by the end of the year. The PSC believes the increase will be attributed to the deregulation of CPE and the divestiture. The PSC also believes the full increase would double residential telephone rates and more than double business rates.

NORTH CAROLINA

Southern Bell has a $143,974,447 rate increase pending. The case was filed on February 8, 1983. The increase is attributed to the FCC depreciation decision and the divestiture. The full increase would raise average residential rates from $11.15 to $17.50, a 57% increase and raise average business rates from $29.61 to $40.99, a 38% increase.

NORTH DAKOTA

Northwestern Bell is expected to file a rate increase request on July 22, 1983. The PSC believes the increase will be attributed to the FCC access charge decision and the divestiture.

OHIO

Ohio Bell has a $179,838,000 rate increase pending. The case was filed on April 1, 1983. The increase is attributed to the FCC access charge decision and the divestiture. The full increase would raise residential rates from an average of $9.00 to $13.10, a 45% increase and raise business rates from an average of $22.58 to $28.18, a 25% increase.

OKLAHOMA

Southwestern Bell has a $301 million rate increase pending. The case was filed on June 24, 1983. The increase is attributed to the FCC access charge and depreciation decisions, the deregulation of CPE and the divestiture. The OCC will rule on the request by mid-October.

OREGON

Pacific Northwest Bell was granted a $36.4 million increase on a non-annual basis on March 30, 1983. It had requested $73.9 million. The increase is attributed to the FCC depreciation decision, the deregulation of CPE, the divestiture and Computer II. The full increase is expected to raise both residential and business rates by about $3.00 monthly.

PENNSYLVANIA

Bell of Pennsylvania has a $378 million increase pending. The case was filed on March 29, 1983. The increase is attributed to FCC decisions, the deregulation of CPE, the divestiture, and normal increases in operating costs. The full increase is expected to raise residential rates by 62% and raise business rates by 38%.

RHODE ISLAND

New England Telephone and Telegraph has a $21,139,000 increase pending.

SOUTH CAROLINA

Southern Bell has filed a letter of intent to file for a rate increase. The PSC believes the increase will be attributed to the FCC access charge and depreciation decisions, the deregulation of CPE and the divestiture. The full increase is expected to raise local rates by 95%. Intrastate long distance rates are expected to drop by 30%. The PSC expects the increase to affect residential customers more than business customers.

TENNESSEE

South Central Bell has a $280 million increase pending The case was filed in July, 1983. The inrease is attributed to the FCC access charge and depreciation decisions, the deregulation of CPE and the divestiture. The full increase would raise residential rates from an average of $12.35 to $31.00, a 151% increase and would raise business rates from an average of $38.55 to $74.50, a 93% increase. The PSC predicts that the full increase would cause 15 to 35 percent of the population to discontinue telephone service.

TEXAS

Southwestern Bell has a $1.0 billion increase pending. The case was filed in June, 1983. The increase is attributed to the FCC access charge decision, the depreciation decision ($450 million of the increase), the divestiture and the loss of the long distance subsidy. The full increase would raise average urban monthly residential rates from $10.75 to $30.75, a 186% increase and would raise average monthly business rates from $27.50 to $37.75, a 37% increase. The Texas PUC is expected to decide the case by February, 1983.

UTAH

Mountain States Bell has a $43,961,000 rate request pending. The case was filed in May, 1983. The increase is attributed to the FCC depreciation decision and the deregulation of CPE.

VERMONT

New England Telephone and Telegraph has a $16 million increase pending. The case was filed on December 1, 1983. The increase is attributed to normal increases in operating costs. Residential and business rates are expected to increase at equal rates. The PSB expects New England Telephone to refile around 1/1/84.

VIRGINIA

Chesapeake and Potomac Telephone of Virginia was granted a $63,826,000 increase on April 5, 1983. It had requested $133,497,105. The increase is attributed to normal increases in operating costs. The increase is expected to affect residential and business customers equally. The SCC expects C&P to file another rate increase request by mid-August, 1983. The SCC believes this increase will be attributed to the divestiture.

WASHINGTON

Pacific Northwest Bell Telephone was granted a $71 million increase in April, 1983. The increase is attributed to the FCC depreciation decision. The increase is expected to affect residential and business customers equally. The UTC expects Pacific Northwest to file another rate increase request around 1/1/84. The UTC believes the increase will be attributed to the FCC access charge decision, the deregulation of CPE and the divestiture.

WEST VIRGINIA

Chesapeake and Potomac Telephone of West Virginia is expected to file a rate increase request in August, 1983. The PSC expects the increase to have a greater impact on residential customers than on business customers.

WISCONSIN

Wisconsin Telephone Company was granted a $55,113,000 increase on May 24, 1983.

WYOMING

Mountain States Bell was granted a $2.6 million rate increase. The increase is attributed to the FCC access charge and depreciation decision, the divestiture and normal increases in operating costs.

SUMMARY OF LOCAL TELEPHONE RATE INCREASES

[A—1982 increase; B—1983 increase; C—anticipated increase]

State	1982 increase	1983 increase	Anticipated increases	Stated rationale						
				FCC access charge decision	FCC depreciation decision	Deregulation of CPE	AT&T divestiture	Long-distance competition	Loss of long-distance subsidy	Normal increases operating expenses
Alabama		[1] $117,000,000	C	C	A	C	C			A
Alaska										
Arizona		[2] 79,000,000						B		B
Arkansas		[2] 138,000,000		B	B	B				
California		[2] 1,400,000,000		B	B		B			B
Colorado		[1] 38,000,000	C		B		C			
Connecticut	[1] $89,024,000		C				C			A
Delaware		[2] 25,900,000		B	B		B			
District of Columbia		[2] 82,000,000		B	B		B			
Florida		[1] 113,000,000								B
Georgia		[2] 158,463,000			B	B				B
Hawaii	[2] 82,368,000				A	A				
Idaho	[2] 34,000,000		C		C					A
Illinois		[1] 21,000,000								B
Indiana		[2] 96,000,000		B		B	B			
Iowa		[2] 68,800,000				B				
Kansas		[2] 213,000,000								B
Kentucky			C							
Louisiana			C	C	C					
Maine		[1] 11,400,000	C				C			
Maryland		[2] 218,000,000		B		B	B	B		
Massachusetts			C	C						
Michigan	[2] 550,000,000			A	A	A				
Minnesota		[1] 56,000,000	C							
Mississippi			C	C	C					
Missouri		[2] 254,000,000		B	B	B	B			
Montana		[2] 20,710,000		B		B				B
Nebraska		[1] 8,033,000	C	C	B	C	C			
Nevada		[1] 5,857,000	C	C			C			B
New Hampshire	[1] 8,380,000		C	C			C			A
New Jersey	[2] 245,000,000		C		A		C			A
New Mexico		[2] 86,100,000		B	B	B	B			
New York			C			C	C			
North Carolina		[2] 143,974,447			B	B				
North Dakota			C	C			C			

SUMMARY OF LOCAL TELEPHONE RATE INCREASES—Continued

[A—1982 increase; B—1983 increase; C—anticipated increase]

State	1982 increase	1983 increase	Anticipated increases	Stated rationale: FCC access charge decision	FCC depreciation decision	Deregulation of CPE	AT&T divestiture	Long-distance competition	Loss of long-distance subsidy	Normal increases operating expenses
Ohio		[2] 179,838,000		B			B			
Oklahoma		[2] 301,000,000								
Oregon		[1] 36,400,000			B	B	B			
Pennsylvania		[2] 378,000,000				B	B			B
Rhode Island		[2] 21,139,000								
South Carolina			C	C	C	C	C			
South Dakota		[2] 21,500,000					B			B
Tennessee		[2] 218,000,000		B	B	B	B		B	
Texas		[2] 1,000,000,000		B	B		B			
Utah		[2] 43,961,000			B	B	B			
Vermont	[2] 16,000,000		C	C	C	C	C			
Virginia		[1] 63,826,000	C				C			
Washington		[1] 71,000,000	C		B	C	C			
West Virginia			C	C						
Wisconsin		[1] 55,113,000								
Wyoming			C	C	C		C			C

[1] Granted.

[2] Pending.

Senator RIEGLE. That will be helpful, and I would like the response of the Commission to that. In other words, does that appear to be accurate? Do you quarrel with the methodology? And if so, how?

I do not mean for you to respond this minute, but I want you to respond for the record on that specifically, because I want to move on to something else.

I would like to suggest to you and to the Joint Committee gathered here that we ask for an entirely different timeframe for the Commission's study to be done. In other words, December 1 as a deadline is unworkable. I think we have got to have a study in here within 30 to 60 days.

Chairman PACKWOOD. I will say again, we will have as many facts as we can get. It is my hope to move along before December 1st, because their access charge goes into effect on the 1st of January.

Senator RIEGLE. That is exactly the point.

Chairman PACKWOOD. If it is going to go into effect—and I hope it does not. Companies are planning for it and states are planning for it. We have got to give them more than a day's notice to say stop.

Senator RIEGLE. I would hope that we could reach an agreement officially to ask that a study be completed within a set period of time. I have suggested a range from 30 to 60 days, but I do not think it can be any longer than that and still give us a turn-around time to be able to write law competently.

So we are going to have to settle that among ourselves, but I just want to put that on the table and hope we can press ahead.

Let me ask you one other question before my time expires, and that is, in your own view what do you think basic telephone service ought to cost to people in this country? I mean, what is a fair dollar figure? To a citizen out there, whatever their circumstances, and particularly those in tough financial circumstances, the bottom line for them is what is it going to cost to have a phone in their house and to use it.

Do you feel that the $10 figure that the Governor of Indiana mentioned for basic phone service is about the kind of figure that we ought to be targeting for? If not, what figure would you suggest?

Mr. FOWLER. It is very hard for me to tell you what a figure might be. What should a chairman make? What should a Senator make? These are very subjective things. I do not know if I can give you the answer to that.

It should be something, it seems to me, however, that is set so that we have universal service, and that typically is defined as 90 to 95 percent of our households with phone service. Now, some of those, just because of their geographic location, cannot get phonelines installed. But there are others, undoubtedly, who just do not have phone service.

Senator RIEGLE. But you must have done studies, and you have to be as knowledgeable, hopefully, as anybody we might ask in the country on this question. What do your economic studies tell you in terms of what is the crossover point in terms of the charge per month where you start seeing a large number of disconnects? Certainly, you should be able to tell us that.

Mr. FOWLER. I will ask Jack Smith to answer that.

Mr. SMITH. The FCC has not done any studies on that specifically. There are studies done by other people, but they are largely very unsatisfactory and not based on concrete data.

One of the things we have asked for and why we need more time for the study from the Michigan petition is, we have asked the States to give us the studies that they had on dropoffs due to actual increases that have actually taken place there.

Senator RIEGLE. I think you have got to do this. My time is up, but I do not understand how we can just be so academic and detached from the effects of these decisions. It's not healthy that we find ourselves at this late hour without any necessary internal information with respect to at what point people drop off the system.

Mr. FOWLER. It is very hard to know that, sir.

Senator RIEGLE. I am not saying it is not hard to know it, but I am just saying that it is up to people like yourself to make these determinations.

Mr. FOWLER. There have been studies that have been done, but they are not satisfactory and that is what we are trying to deal with right now in cooperation with the States.

Senator RIEGLE. But you have not done one internally, as I just heard this witness say.

Mr. FOWLER. No, we have not.

Senator RIEGLE. And that to me is a surprise. I am surprised we would be this far down the track and that kind of very fundamental piece of work would not be done.

Mr. **Fowler**. Not when you consider we are talking about a $2 a month rate increase in 1984. But we are getting that information in, sir.

Chairman **Packwood**. Mark, let me say this. It is very clear—I was just talking to Chairman Dingell—that he is prepared to move on this, he said, much before 60 days. Whatever you can get, our staffs will be on top of you and with you, but it is our intention to try to move in September.

Mr. **Fowler**. I understand, sir, and I would be glad to work with you. I do not know how we can make the States, for example, respond faster, because we want to get the information from all of the States. And so a lot of our ability to respond will depend upon how fast the States can respond or will respond.

[The statement follows:]

STATEMENT OF HON. MARK S. FOWLER, CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION

Mr. Chairman and Members of the Committee: I welcome the opportunity to appear before you today to address our common concerns about the affordability and availability of telephone services, the continued strength of the telecommunications industry, and the vitality of our economy and society as we progress into the Information Age.

INTRODUCTION

There are several points which I will stress in my testimony and at the outset I would briefly like to outline these points. First, the Congress and the Commission are working to achieve common goals—we want to make sure that high quality telephone service is maintained at reasonable prices to all the people of the Nation. We also wish to promote the efficiency and vitality of the telecommunications industry so that it may continue to play a leading role in the national economy and support the international competitiveness of the United States.

Second, attention has been focused upon the possible effects of the Commission's access charge decision largely because of the recent flurry of local rate increases requested by many telephone companies. The $2.00 monthly charge imposed by the access charge decision in 1984 will have only a minimal effect on consumers, when compared with the local rate increases now being sought from state regulatory bodies, and the Access Charge Order will be no excuse for the large rate hikes sought from many state regulatory bodies. It should be obvious, for example, that the Commission's $2.00 access charge cannot be used as justification for the $20 rate hike Southwestern Bell is seeking in Texas. Also, since MTS usage rates will decline under the access charge plan, many subscribers will not suffer any net increase in rates as a result of the Commission's decision, but in fact may experience a net reduction in total charges. Although portions of these rate increase requests may be justified to reflect inflation and changes in carrier's operating costs and to accommodate recent regulatory and judicial actions, I suspect that a hefty portion of these proposed increases may be traced to an effort by the local companies to use the dramatic changes occurring in the industry as an excuse to seek higher rates than otherwise would be warranted.

As I will describe in my testimony, the Commission is committed to examining expeditiously the facts surrounding these rate increase requests in an effort to determine the extent to which they can be justified by the companies. State commissions will be performing a similar function in their ratemaking proceedings. It is important to keep in mind that any congressional reversal of the access charge decision will barely land a glancing blow at the target of these pending local rate increase requests.

Third, the Access Charge Order will generate enormous savings to society through more intensive and efficient use of the interstate network. At the same time, it has a number of built-in safeguards to preserve universal service. Further, as I have mentioned, the decision will have only a small impact on consumers' pocketbooks and, in fact, will benefit many consumers.

Fourth, there will be ample time to assess and correct any unexpected adverse effects stemming from access charges. As my testimony will indicate, the Commission intends to monitor closely the implementation of the access charge plan to ensure that any adverse impacts can be averted quickly. Further, the Congress obviously can revisit this issue through oversight or targeted legislation after there is more reliable information demonstrating the effects of access charges which may form a basis for congressional action. The access charge plan is, I believe, well thought out, is supported by an extensive record based on five years of proceedings, and ought to be given a chance to work. I do not believe that current developments make it necessary for the Congress to act at this time. More importantly, such action could run the risk of locking into place attempted solutions which ultimately will upset the delicate balances needed to sustain the dynamic changes reshaping the telecommunications industry. Pricing inefficiencies in the name of universal service carry the risk not only of failing to achieve their express telecommunications policy goals, but also of adversely affecting all of the social and business activities which rely on this very important sector of the United States economy.

Finally, the Commission needs the flexibility wisely extended to us by the Congress in the Communications Act of 1934 to cope with a fast-changing industry. This flexibility would permit the Commission to alter the access charge plan to address unforeseen circumstances, unexpected adverse effects, and new services and technologies which undermine continued achievement of the statutory goals. The Congress therefore should be cautious in framing legislative solutions, in response to concerns over possible local rate increases, which will be difficult to alter and which could quickly be made obsolete by the dynamics of the telephone industry.

BACKGROUND

The Access Charge Order adopted by the Commission in December of last year revised procedures for compensating local telephone companies for their participation in interstate and foreign services, and similar approaches to compensation of local telephone companies for their participation in state toll service are being considered in the various states. Because of your proper concern whether these new rate procedures will affect the wide availability of telephone service, you are considering various legislative proposals which bear on access charges. I will address the Commission's access charge decision and the significant refinements which were adopted yesterday in some detail. But first, I would like to discuss our common concerns and demonstrate how the access charge decision represents a sensitive balancing among disparate policy objectives.

The touchstone of the Commission's treatment of access charges and related matters is the Communications Act, a directive from the Congress which wisely states the multiple statutory objective that there should be available "so far as possible, to all the people of the United States a rapid, efficient, Nation-wide . . . service with adequate facilities at reasonable charges. . . ." It is our responsibility under the law to promote this objective. In formulating our access charge decision, and in developing related jurisdictional separations decisions in cooperation with state regulatory commissions, we have translated this objective into four discrete goals:

Preservation of widely available telephone service at reasonable charges (a "universal service" goal).

Promotion of network efficiency.

Limitation of uneconomic bypass.

Elimination of unjust and unreasonable discrimination among services and service providers.

We have achnowledged that there is some tension among these goals, and that any access charge plan (and any related plan for treatment of jurisdictional separations) of necessity would represent a difficult compromise. The particular compromise embodied in the Commission's access charge plan, as modified yesterday, is the product of five years of proceedings and comprehensive comment filed by carriers, state regulatory bodies, and user and consumer groups. It also should be noted that the Commission's action has been supported by large segments of the industry and other groups filing comments. Local exchange carriers, including all the Bell Operating Companies, have expressed strong support for the access charge plan. Other supporters of the general thrust of the Commission's policies in the Access Charge Order have included AT&T, Centel, GTE, Continental, the Ad Hoc Telecommunications Users Committee, and MCI.

CHANGES AND PRESSURES IN TELECOMMUNICATIONS

All of us are aware of the fact that dramatic and far-reaching changes are reshaping the telecommunications industry. The efficiencies of new technology are being brought to the public in innovative terminal equipment, network services, and unregulated enhanced services at an ever-increasing pace as we progress into the Information Age.

Whole industries depend directly upon telecommunications in connection with their offering of services and products to the public, and all of domestic and international business depends upon telecommunications to conduct business. Telephone toll service revenues were approximately $44 billion and local service revenues were approximately $35 billion for domestic companies last year. Domestic satellite revenues were over $300 million last year and are expected to exceed $1 billion annually during this decade. Domestic companies shipped over $14 billion in telephone and telegraph equipment in 1982, including exports of approximately $725 million. These equipment revenues are expected to rise in the future. Telecommunications equipment and services rank third behind agriculture and aerospace technology as the leading exports of the Nation.

The telecommunications industry also is a major source of jobs—the Bell System alone accounts for over 1 million employees. Further, the burgeoning computer industry is becoming increasingly reliant upon telecommunications for the transmission of data. The growth of this industry has been spectacular—last year, personal computer sales alone accounted for 2.8 million units. A strong telecommunications industry is essential to maintain this pace of growth in the computer field. The Nation is rapidly evolving from an economy based upon smokestack industries to one based upon information services. In the process, thousands of new jobs are being created and the productivity of the Nation is improving markedly. Further, the impetus to telecommunications provided by lower, competitively priced long distance rates which will result from the access charge decisions, could lead to the development of completely new information uses or even industries in the next decade.

A great deal is at stake. We must ensure that this core sector of the economy be allowed to play its full role in promoting a productive, efficient economy and in improving the American standard of living. The choices we make will have a direct and far-reaching impact on the telecommunications industry itself, upon all aspects of our economy and society which rely upon telecommunications, upon the international competitiveness of the United States, and upon the people of this Nation. It is critical that policies are adopted which carefully consider the sound development of the complex and dynamic telecommunications industry and the industries which rely on it.

The development of competition and new entry in the long distance telephone market have created pressure for changes in the industry because they have had the effect of throwing out many of the rules and procedures under which service was traditionally provided and costs were recovered in a monopoly setting. This competition, and related competition in the customer premises equipment market, has been nurtured by decisions of the Commission and the courts, and has brought significant benefits to residential and business consumers of service. These benefits have included increased productivity, jobs, and a greater diversity of products and services at affordable prices. But competition also has recast the landscape of the industry by introducing new pricing and service alternatives to the traditional monopoly service offerings which have made established pricing practices difficult or impossible to sustain in the future.

Local telephone companies participate in the provision of the interstate and foreign services subject to the Commission's jurisdiction. They provide the local "tails" to such long distance services, and under decisions of the courts they are entitled to compensation for the use of their facilities in interstate and foreign calling. In the past such compensation was largely the product of negotiation by the involved traditional telephone companies, a process which has proved ineffective when new providers of long distance services emerged and the local telephone companies had little incentive to agree to such "partnership" compensation procedures.

Most significantly, among the facilities for which local telephone companies are entitled to compensation are the non-traffic sensitive costs of local loops, premises wiring, and terminal equipment. It is critically important to an understanding of the access charge decision to keep in mind that the costs of these facilities do not change with usage; a loop costs the same if it is not used at all, or if it is used continuously. Yet, the monopoly pricing for long distance service historically covered the interstate cost of these facilities solely through usage charges, which had the effect of requiring excessive compensation for use by large users of interstate service, and inadequate compensation for use by others.

The problem with this system is that it created economic and technological inefficiencies. Large users of telecommunications would pay many times their share of NTS costs and have sought service alternatives such as private lines which avoid the usage-based charges for use of local facilities. New long distance entrants have sought to mask their service offerings as private lines similarly to avoid such charges. The users of traditional MTS and WATS long distance services make up the difference. As a result of artificially high prices, users in general made fewer long distance calls.

Under the Commission's access charge plan these forms of unfairness will be corrected over time. Just as other utilities (such as gas and electric suppliers) which are subject to competitive alternatives have separated out "system connection" from "usage" charges, to ensure that users of competitive alternatives are not subsidized by those who do not have such alternatives available, in telecommunications we similarly must move toward such cost-based pricing approaches. Only then will the full benefits of true competition be realized—competition predicated upon better products tailored to consumers' needs, and not competition on how best to escape uneconomic pricing policies of traditional suppliers. We believe that when this is properly explained to the public, the American people will recognize that the existing system is not equitable, and that the approach of the access charge plan will be more fair.

Furthermore, the traditional use of usage-based charges to recover fixed non-traffic sensitive costs has had the effect of inflating long distance service rates above the actual cost of providing such service. This has effectively suppressed demand for interstate and foreign services, thus creating inefficiencies in the use of the public switched telephone network. Thus, potential customers are artificially discouraged from taking advantage of the many useful services created by the ongoing merger of telecommunications and data processing technologies. As the Nation moves into the Information Age, we cannot afford to sacrifice the benefits to the national economy and to our society that modern telecommunications-related services can provide due to artificially inflated toll rates.

An additional pressure has been created by the Modification of Final Judgment (and a similar decision regarding the acquisition of Southern Pacific Communications by GTE). The Modification requires the BOCs to file non-discriminatory cost-justified tariffs for exchange access to take effect in connection with divestiture, and it requires termination of the contractual compensation procedures ("division of revenues") long employed in the integrated Bell System to compensate the local telephone companies for their participation in long distance calling. This has created pressure for expeditious action by the Commission, prior to the scheduled January 1, 1984, divestiture date, and pressure toward "cost-justified" pricing policies.

The growing tendency of large users of interstate services to bypass exchange facilities to avoid traditional usage-based charges for use of these facilities also is threatening the efficiency and continued viability of the public network. Large users joining the ranks of bypassers include Citicorp, Westinghouse, Boeing, Las Vegas casino owners, and numerous state and local government agencies. Since large users would pay a disproportionate share of the non-traffic sensitive costs under the current system through MTS charges, they have had great incentives to utilize alternative services and facilities to avoid uneconomic charges. And, as a byproduct of divestiture, AT&T itself could become the largest potential bypasser of local exchange facilities.

The means for bypass have become available through the recent onrush of technology, including satellites, optical fiber, microwave radio, coaxial cable, cellular radio, and traditional paired wire cables. Some of the bypass systems already constructed have not been efficient investments in that their costs exceed the costs of local telephone companies' exchange plant which could have been used, but the distorted rates for use of the exchange plant have encouraged such uneconomic investment. It makes little sense to maintain ratemaking policies which have the effect of creating incentives for bypass artificially when bypass is *not* the cheapest way to transmit information. But this is exactly what the current system is doing. Large users which are the most immediate candidates for use of bypass systems have provided large amounts of support for local telephone services in their areas. If they accept the administrative and cost burdens of constructing bypass facilities, they will tend to maximize their use of such facilities and largely avoid use of the local telephone companies' exchange facilities. The net result will be that remaining subscribers, including residential and small business subscribers, will be forced to make up the difference and be stuck with higher costs per line for exchange plant.

In sum, the current system suffers from built-in inequities and inefficiencies which are harmful to all consumers and which threaten greater harm in the future. Because of bypass and other competitive realities in the current telecommunications market, the Commission has sought to minimize uneconomic pricing and discrimination, while maintaining consistency with statutory objectives, in a manner which carefully balances economic efficiency with universal service objectives and which minimizes incentives to construct and utilize uneconomic bypass systems.

THE FCC'S MODIFIED ACCESS CHARGE PLAN

The Communications Act properly and wisely charges the Commission with the responsibilities of fostering development and maintenance of a rapid, efficient, nationwide telecommunications service which is widely available at reasonable charges. This latter goal of relatively universal service was pursued in the monopoly environment by toleration of the inefficiencies of excessively high toll rates as a means of holding down flat-charge local service rates in the belief that such a cross-subsidy of local rates contributed to the widespread availability of telephone service. This approach certainly made sense in the 1930's and thereafter when telephone service was not universally available, when rural sections of this country did not have service, and when a major policy goal of the Nation was to ensure that service would be made available rapidly to the unserved. The Congress also aided in this effort, for example by making Rural Electrification Administration guaranteed loans available to telephone companies after 1949.

But the time has come to recognize our joint success. Telephone service is available universally today at reasonable charges. Penetration rates exceed 95 percent in virtually all regions of the Nation. The issue today is not whether telephone service should be made available initially to the public, but rather whether, in the light of all of the inflationary and other pressures driving all utility rates up, material numbers of subscribers will be forced to discontinue telephone service. We are confident that the access charge plan—which does *not* represent a rate increase to broad groups of subscribers—will not cause subscribers to disconnect from the phone system.

The basic philosophy of the access charge plan ultimately is to cause usage-based long distance rates to fall and to cause subscribers to cover the fixed non-traffic sensitive costs with flat charges. We have recognized that this represents a change in the way telephone bills have been rendered, and we have carefully adopted transitional procedures to ensure that residential subscribers will have an opportunity to get used to these new ratemaking procedures. As I will discuss, residential subscribers will pay a fixed monthly charge of $2.00 in 1984, which will rise to $3.00 in 1985 and $4.00 in 1986. The remainder of the costs of their non-traffic sensitive facilities will continue to be covered in long distance carriers' usage-based charges. We believe that, as a practical matter, a $2.00 (or $4.00) charge will not materially affect decisions by residential subscribers to retain telephone service. Further, state regulatory authorities have flexibility under the access charge plan to require telephone companies to offer low-cost life line type services to subscribers. If this is done, few people will be induced to leave the system.

But, we do not rest on the assumption that the effects of the access charge plan will be minimal. We will be continuously monitoring implementation of the access charge plan, related changes in jurisdictional separations procedures, and the transitional procedures adopted in both areas, to determine whether changes are warranted. As I noted earlier, this is the flexibility that the administrative process makes available: warranted changes can be made quickly, to minimize adverse effects on the public.

The access charge decisions promote equity and efficiency by providing that all customers will pay their fair share of the fixed costs which are directly attributable to their telephone service. Some critics of the Commission's action have argued that it makes subscribers pay for services they do not use by imposing a flat charge for access to the interstate long distance network on all subscribers even if they do not make any interstate toll calls. But, as I have explained, the facilities connecting subscribers to the switched network are dedicated to the use of each individual subscriber. These costs are fixed and do not vary with usage. Recovering most of these costs through flat charges—subject to the kinds of protections for universal service which I will describe—is entirely fair.

Critics of the Commission's decisions still may argue that we should be less concerned with considerations of fairness because most heavy users of the interstate toll network are big businesses which are well positioned to subsidize residential customers, especially since some of these customers are needy or elderly persons. Although all of us are striving to maintain a communications system which provides reasonably priced service to all segments of our society, we must be very careful in assessing this sort of argument. The current system subsidizes *all* local rates, not just those of the truly needy. And the current system does not target specific rate support to high cost areas. We should deal with our concerns for the truly needy and service in high cost areas in a straightforward, targeted manner which avoids significant rate distortions and does not threaten the quality of telephone service all of us receive. A second problem with this argument is that it ignores the fact that these large interstate toll users have alternatives available—they can avoid the public network by using facilities which bypass the local exchange.

The Commission's access charge decisions promote network efficiency by reducing incentives for bypass and bringing toll rates in line with usage costs. This is achieved by lowering the amount of the interstate portion of local costs which is recovered through interstate toll charges. Our staff estimates that, as a result of this shift in cost recovery, interstate long distance rates should initially decrease by approximately 15 percent for all residential customers and businesses. The Commission will have authority to take necessary action to ensure that these rate reductions are made available equitably to all users of long distance service.

Specific actions taken by the Commission yesterday on reconsideration of the December access charge decision will assist in lowering MTS long distance rates applicable to residential and business customers. For example, the Reconsideration Order imposes a surcharge (with certain exceptions) upon the closed end of private lines and WATS access lines to compensate for their use of exchange facilities. The surcharge, which should amount to approximately $25 per closed end, will further aid in reducing MTS rates. Other actions taken in the Reconsideration Proceeding will help ease upward pressures on local rates. Under the original Order, Centrex-CO access lines were considered to be treated the same as other business access lines and would have been subject to a $4.00 flat charge for each line obtained by subscribers to Centrex-CO service. The problem with this approach was that many subscribers to Centrex-CO service may have viewed the service as prohibitively expensive because of the imposition of these access charges. If a significant portion of these customers dropped their Centrex-CO service the telephone companies would have been left with large investments in Centrex-CO equipment which no longer was generating revenues. This investment would have been recovered through increases in other local rates. The Commission, I believe, has avoided this problem upon reconsideration, by pricing the flat charge for Centrex-CO service at the residential flat rate, rather than at the higher business rate. This pricing should reduce pressures which otherwise would have been generated for local rate increases, while also affording Centrex-CO users the time to make reasoned decisions to use alternative equipment or continue to subscribe to Centrex-CO.

Several features in the access charge decision and the recommendations of the Joint Board in the Jurisdictional Separations Proceeding advance the objective of universal service. Ensuring protection of telephone subscribers while moving to a more efficient and equitable method for recovering local exchange costs has been one of the Commission's primary goals in the Access Charge Proceeding. We have taken four basic steps to achieve this goal. First, we have provided for a gradual transition to the new access charge environment so that consumers will have time to adjust to the new method of recovering the interstate allocation of local exchange costs. Second, the Commission has limited the amount of local exchange costs to be recovered from subscribers at the end of the transition period. Third, the Commission has established a Universal Service Fund to be paid for by interexchange carriers, and asked the Joint Board in the Jurisdictioanl Separations Proceeding to prepare recommendations concerning the level of funding necessary to ensure the continued availability of telephone service in high cost areas. Finally, we have provided for careful monitoring of access charge implementation to ensure that the anticipated benefits are realized and that we have ample opportunity to make any adjustments necessary to avoid adverse effects. I would like to discuss these features in greater detail, with particular attention to the ways in which we intend to safeguard universal service.

First, as a result of the Reconsideration Order adopted by the Commission yesterday, end user usage charges will be eliminated and the flat fee for residential customers will be set at $2.00 for 1984, $3.00 for 1985, and $4.00 for 1986. Under the original Order, the *minimum* flat fee for residential users was $2.00 for 1984 and the maximum for that year could have been as high as $4.00.

It is instructive to put these figures in perspective. While this by itself does not justify a price increase, telephone service is and will remain one of the greatest bargains consumers enjoy, as compared with the costs of other vital goods and services. Adjusted for inflation, the cost of phone serice has actually fallen by more than 30 percent between 1972 and 1981, and even in nominal dollars has increased only 30 percent during that period, a far lowr increase than that in any other major class of consumer expenditure over that time. For example, between 1972 and 1981 prices for most other goods and servics have increased dramatically: food 107 percent, medical care 118 percent, gas and oil 277 percent, fuel oil and coal 472 percent. This reflects the dramatic productivity and efficiency gains made possible under regulatory policies which have nurtured the rapid introduction of new services and technologies in telecommunications.

We have heard considerable talk recently that the Commission's policies threaten to divide the Nation between "haves" and "have nots" in terms of the availability of high quality telephone service. Certainly, none of us would want this to happen, but it is hard to point to any evidence that we are facing such a risk. The phone bill is only a small fraction of the average household's expenditures. In 1981, telephone and telegraph services made up only 1.7 percent of all personal consumption spending. The percentage for food and tobacco was 22 percent, medical care 11 percent, and household energy utilities 5 percent. Since telephone service costs make up such a small percentage of household expenditures, it is obvious, that the effects of the Commission's access charges will be virtually insignificant. Further, the refinements we have made on reconsideration regarding flat fee rates will directly aid consumers by easing the transition to cost-based rates.

As a second feature to protect universal service, we have provided that certain types of NTS exchange costs will *never* be transferred to end users. These include costs relating to embedded customer premises equipment, inside wiring, and a portion of central office equipment. Under the so-called "Pure II" approach which was recommended during the access charge proceeding *all* NTS costs would have been shifted to end users. But we have rejected this approach in order to protect universal service.

Third, the modified Order provides that the change to flat fees for the recovery of NTS costs will not be carried out immediately but rather will be phased in over a 6-year transition. This obviously does not constitute an "abrupt" transition, although there have been attempts to characterize it that way.

Fourth, the recommendations of the Joint Board in the Jurisdictional Separations Proceeding will result in a further safeguarding of universal service. As I have mentioned, the Commission requested the Joint Board to prepare recommendations for changes in separations procedures to protect subscribers in high cost areas. The Joint Board, composed of four state regulatory commissioners and three members of the Commission, adopted basic recommendations for changes in jurisdictional separations at its April 15, 1983, meeting. The full text of the Joint Board's decision will be released in the near future.

Under the present system, the proportion of local exchange costs allocated to the interstate jurisdiction varies from company to company since the interstate allocation is a function of the relative level of interstate calling. As a result, some subscribers pay more of their local exchange costs through local exchange rates than others. The Joint Board has recommended that all companies allocate 25 percent of their NTS local exchange costs to the interstate jurisdiction. Most of these costs will eventually be recovered directly from telephone subscribers under the Commission's access charge plan.

The Joint Board has recommended, and I support, a requirement that interexchange carriers help pay the cost of local telephone plant in high cost areas through a Universal Service Fund. This will reduce the *intrastate* revenue requirement and allow lower local rates in high cost areas. This rate support would be available to all companies with NTS costs more than 15 percent above the national average. It would cover, at a minimum, half of the costs above this level. this percentage of covered costs is substantially greater in higher cost areas. The Joint Board also has recommended capping the access charge mandated by the Commission so that no subscriber would pay an interstate access charge which is more than twice the national average. The full package of subscriber protection recommended by the Joint Board requires interexchange carriers to pay almost all NTS local exchange loop costs in excess of twice the national average.

These recommendations were endorsed by all four state commissioners on the Joint Board. These provisions will provide a substantial amount of protection for telephone subscribers in high cost areas. At the same time, these recommendations are carefully tailored to avoid reintroducing incentives for inefficiencies in using interstate services.

A fifth protection is the extensive monitoring requirements we have adopted. The monitoring procedures will enable us to make necessary adjustments to protect universal service. The Access Charge Order, as modified, requires the Commission, before the end of the third year of the transition, to evaluate the impact of access charges in order to make changes in the system to protect universal service. Also, the Commission yesterday voted, in response to a petition filed by the Michigan Public Service Commission, to examine currently pending local rate requests, gather data regarding the potential effects of recent federal actions on local service rates, and prepare a report by December 1, 1983. This action by the Commission also is responsive to concerns expressed in House Resolution 231.

We also have begun action to establish an access monitoring plan to protect universal service. Information regarding rates and the number of residential access lines will be collected annually during the transition period. This will enable us to assess rate trends and determine whether residential disconnects are increasing. This will serve as a warning system enabling us to make necessary changes to protect universal service. Also, the Joint Board in the Jurisdictional Separations Proceedings has recommeded that it be given ongoing authority to monitor the effects on universal service of both the separations changes and the access charge plan.

Finally, the Order allows carriers to seek a waiver of the requirement that end user charges be imposed in response to targeted life line services which may arise on the state level. This represents a mechanism under which new charges may be avoided for the truly needy.

PENDING LEGISLATIVE PROPOSALS

I would like to devote the balance of my statement to some brief comments regarding pending legislative proposals affecting the access charge decision and sparations recommendations, as well as some other proposals relating to our regulatory decisions and authority. Let me begin by reemphasizing that many of the concerns addressed in the various bills before you have been addressed in the Commission's access charge decisions, just as they were by the many parties filing comments during the five years of proceedings which led to adoption of these actions.

First, several proposals would keep the current system in place and then ultimately replace it with an access charge system which continues to use interstate toll rates to subsidize local costs. I am concerned, as my previous testimony has indicated, that such an approach could allow the problems of economic inefficiency and bypass to continue to grow. Delay in facing up to these problems could make dealing with them down the road much more difficult. Further, keeping the current system in place may conflict with the operation of the MFJ. The MFJ requires a new system of cost-based access charges and there is considerable pressure to have this new system in place at the time of divestiture. The legislation, by proposing to leave the current system in place for up to two years, is not consistent with the MFJ because the MFJ eliminates the present division of revenue agreements between AT&T and the BOCs. This inconsistency could cause considerable confusion unless the matter is specifically addressed in legislation.

Second, several proposals would establish a Universal Service Fund similar in concept to the Fund recommended by the Joint Board, and funded under the access charge decisions through carriers' payments toward support of high cost exchanges. It is essential that any legislative requirements for calculating high cost and providing for their recovery do not magnify the problems of inefficiency and bypass which I have discussed, or diminish incentives for exchange carriers to innovate and use efficient facilities and procedures to provide service. If the Fund is required to carry too great a burden in subsidzing local service costs, interstate toll rates will go up and interexchange carriers and large users will be driven toward alternatives which avoid such support. Your Committees should be very careful in reviewing whether proposed legislation makes a realistic assessment of the load which can be placed on interstate toll rates.

One proposal, for example, would permit local telephone companies to recover 90 percent of that portion of their costs exceeding 110 percent of the national average, and 100 percent of their costs over 250 of the national average. This formula would require approximately $840,000,000 annually for the Fund, compared to approximately $395,000,000 under the Joint Board Plan (using 1980 dollars).

Pending proposals also suggest that exchange carriers should be eligible for reimbursement from the Fund if their costs for "intra-LATA" service, rather than strictly local service, exceed the national average. Since intra-LATA service will include a considerable amount of intrastate toll services, such an approach would have the effect of using interstate rates to subsidize long distance services and facilities on the state level. There may be a risk that his expansion of the concept of universal service to cover subsidizing intrastate toll rates could materially increase *interstate* rates by expanding the size of the Fund and cause inefficiencies in the use of interstate services.

Finally, several proposals have sought to deal with the bypass "problem." One approach, for example, would impose a $100,000 fine for bypassing the local exchange. I am concerned that the bypass problem may elude any such direct legislative attempt to stamp it out with criminal or civil penalties. In many cases it is very difficult to identify when bypassing is actually occurring. It could cost the government substantial sums of money to investigate possible violations and to adjudicate the imposition of fines. Also, the proposed legislation applies to "any" transmission of telecommunications which avoids accessing the local exchange. This could be construed as meaning that each plane call is subject to a $100,000 fine, rather than what probably was intended, a single fine for use of the facilities. Further, many carriers and companies already have spent considerable sums of money to set up private communications systems. There is a need to clarify whether any new legislation is intended to bar the continued use of these in-place systems, and to address the difficult issues of what their status will be in the future. Finally, although provisions such as these are proposed to be placed in the Communications Act, it is not clear whether they intended to be a forfeiture or a criminal fine. If a criminal fine is intended, enforcement responsibility would be in the Department of Justice, and not in the Commission. Perhaps this should be clarified in any legislation which might be adopted.

A second proposed legislative approach to the bypass problem is to require persons who bypass local exchange facilities to pay a charge to the local phone company anyway, on the apparent theory that the local exchange serves as an available "back up" for these systems and thus is entitled to their support. But this may be viewed as the same as saying it would be fair to impose a tax on the airline industry in order to subsidize local street construction because the roadways are a "back up" to airline transportation. A potential problem with this approach is that it could hinder technological development and impede productivity in the telecommunications industry. A further problem is a legal one. There is some doubt that local telephone companies in fact could assess a charge on a non-subscriber, when the very nature of service charges is contractual and the bypassers would not have entered such contracts.

The Commission's access charge decisions discourage *uneconomic* bypass—that is, investments in bypass systems which have costs greater than the costs of the exchange plant. But the tax-like approach which is being discussed, unlike the Commission's action, could "throw the baby out with the bath water" by handicapping the development of alternative systems which *are* economically efficient. The strength of this industry is its ability to develop technology for new and better services. Penalizing the development of economic bypass systems, which are a significant spur for improvement of common carriers' systems, could undermine the industry's greatest asset. The Senate, incidentally, in passing S. 66 has sought to promote the development of these economic alternatives by permitting cable companies to provide bypass services.

There also are a number of other legislative proposals pending before your Committees which do not directly relate to the access charge decisions or separations recommendations, but which do affect other Commission decisions and our regulatory authority. I would like to comment briefly on some of these proposals in an effort to assist your committees as you consider legislation.

First, certain of these proposals would overturn actions taken by the Commission regarding the depreciation of telephone company plant. These proposals would permit the states to set their own depreciation rates for facilities used for both local and long distance service. Although the Commission has sought to cooperate with the states as much as possible in the development of telecommunications policies, my concern with this depreciation proposal is that it could undermine the continued development of pro-competitive policies which we have established. The problem is this: Many states have prescribed depreciation rates which extend the capital recovery period beyond the realistic useful life of telephone company assets, and these depreciation rates do not apply to competitors. This approach has denied the phone companies the recovery of their capital investments in a timely manner. This, in turn, has made it difficult for the phone companies to implement new technologies, to price their services efficiently, and to improve and expand their services. This appears to be especially critical to the BOCs which will need to be placed in a position of economic viability after divestiture if continued service is to be maintained to local ratepayers who depend upon these local monopoly entities.

All of this makes it much more difficult for the telephone companies to compete with companies which are not subject to these depreciation schedules, and also slows technological growth. The Commission has acted to establish depreciation rates which provide a more realistic capital recovery mechanism. It is my view that the states should not be given authority to undercut this Commission effort to foster competition and technological innovation.

Second, it has been proposed that the Commission should be required to ensure that rates for basic local telephone service do not exceed 110 percent of the national average for comparable services. It would be extraordinarily difficult for the Commission to devise any national average for basic local service, primarily because there is a proliferation of different types of local service permitted under state tariffs and there is no consensus about which ones are "basic" and which are not. Another potential problem with this approach is that it could dilute the ratemaking authority of state commissions. Their discretion regarding how local costs will be recovered through the ratemaking structure could be limited because the Commission—not the states—would be enforcing a cap on basic local phone rates based upon some undefined national average. It is my view that there is no need to do away with the present federal-state partnership regarding telephone ratemaking. The states have a legitimate role in exercising responsiblity for local phone rates and this role should be permitted to continue.

Third, several bills contain a provision requiring that, contray to the MFJ and the Commission's *Computer II* decisions, embedded CPE will continue to be owned by the BOC's after divestiture and will remain under state tariff until fully depreciated. (Under the MFJ, AT&T would own all embedded CPE after divestiture.) Keeping embedded CPE under tariff, in my view, could run counter to the pro-competitive steps taken by the Commission in its *Computer II* decision. In that proceeding we noted a general consensus that a substantial level of competition has developed in the terminal equipment market, and this finding led us to deregulate the offering of new terminal equipment. We currently are conducting proceedings to deregulate embedded equipment. (Although we have noted in that proceeding that the continuation of state tariff regulation may be an option for certain categories of embedded CPE if the requirements of certain court decisions cannot be satisfied by a detariffing plan, we have stressed our intention to fashion a plan which avoids any need for continued tariffing.) If the terminal equipment market is competitive there simply is no need for further regulatory involvement.

A further concern is that keeping embedded CPE under tariff may not be in the best interest of local ratepayers. Because of growing competition and rapidly changing technology, many telephone customers are turning in their telephone equipment in order to purchase new equipment from other vendors. If embeded equipment remained under tariff, the phone company still might be entitled to recover its investment in this returned equipment through increases in other local rates and, thus, the local ratepayers would bear the burden caused by the loss of the embedded CPE's revenue stream.

Fourth, recent proposed legislation would amend the Communications Act to give the Commission authority to forebear from regulating telecommunications services and facilities if forebearance is warranted by the level of competition. It is my view that such legislation would provide useful clarification of the extent to which the Commission has authority to exercise its discretion to refrain from imposing regulation upon competitive segments of the telecommunications industry. There is no need to impose the full panoply of rate, entry-and-exits, and service regulation under Title II of the Communications Act upon telecommunications companies with limited market power. The view of the Commission has been that Title II of the Communications Act can be fairly construed as being designed to limit the conduct of dominant telecommunications firms, and that the mechanisms of Title II do not promote the public interest when employed with respect to the conduct of firms which do not have market power. Clarification of the Act in this regard would facilitate the continuation and expansion of the pro-competitive policies we have developed.

Finally, it has been proposed that state commissions be given authority to require exchange carriers to lease and maintain on request a single basic one-line telephone and associated inside wiring for subscribers within the state. These offerings would be made pursuant to state tariffs. It is my view that such legislation is not necessary because of action already taken by the Commission. In the *Computer II* proceeding the Commission has consistently indicated its commitment to the belief that marketplace forces can ensure the efficient provision of telephone equipment to all customers. We have recognized, however, that during the transition from a regulated environment to a CPE environment which is governed by market forces there is a potential that disruptions in the provision of CPE to telephone customers may occur. In light of this potential problem we adopted an Order in May 1983 in response to a petition filed by the National Association of Regulatory Utility Commissioners. The Order establishes, on an experimental two-year basis, procedures under which state commissions may require carriers (other than those which are subject to the structural separation requirement of our *Computer II* decisions) to serve as carriers of last resort in the provision of CPE to customers. It is my view that this approach is the surest means of minimizing any risk that disruptions of service may occur during the transitional period while also ensuring that the pro-competitive policies adopted in *Computer II* are permitted to operate. There is no need permanently to require carriers to be subject to tariff requirements regarding the provision of CPE, as is proposed in the legislation. Such an approach, in fact, could impair the continued progression to a competitive CPE market.

CONCLUSION

Let me conclude by emphasizing that all of us can agree on our basic objectives: universal service, efficient use of telecommunications services and facilities, a strong telecommunications industry, and technological growth. The rapid changes in the industry are forcing us to make critical choices, and I believe that the decisions made by the Commission promote the goals of equity, efficiency, and universal service. As your two Committees begin to consider legislation, I urge you to consider carefully the multiple dimensions upon which your policy decisions will bear. We at the Commission are sensitive to the public interest requirements of the Communications Act, and to the concerns you have expressed. In that spirit let me stress that the Commission is anxious to cooperate and assist you in your efforts to achieve these common goals.

I thank you for this opportunity to appear before you today, and I welcome the chance to respond to any questions you may have.

[The following information was subsequently received for the record:]

Federal Communications Commission,
Washington, D.C., August 19, 1983.

Mr. Ward H. White,
Senior Counsel, Committee on Commerce, Science, and Transportation, U.S. Senate,
Washington, D.C.

Dear Mr. White: After reviewing preliminary transcripts of the hearings of July 28, 1983, on telephone pricing policies, Chairman Fowler has asked me to furnish your Committee and the Committee on Energy and Commerce of the House of Representatives an elaboration of certain of his remarks before the Committees.

First, there were several questions regarding the residential flat charges during the last three years of the transitional period under the Commission's access charge plan. This correspondence provides the Senate and House Committees a more extensive explanation of the action taken by the Commission regarding residential flat charges.

The Commission's Reconsideration Order eliminates end user usage charges and provides that, absent any evidence of harm to universal service, all costs assigned to the end user common line element will be recovered through flat end user charges at the end of a six-year transitional period ending December 31, 1989. In 1984 the monthly residential flat charge is set at $2.00. This increases to $3.00 in 1985 and $4.00 in 1986. At the end of the third year of the transition, the Commission will examine the operation of the access charge system to determine whether it has resulted in any adverse effects upon consumers or upon the goal of universal service. If the Commission concludes that no changes in the access charge plan are necessary, then the residential flat charge for the remaining three years of the transition would be determined as follows: At the beginning of each of the three years 25 percent more of the remaining common line revenue requirement would be shifted to end users; the remaining 25 percent would be shifted at the beginning of 1990. Thus, 100 percent of the common line element would be paid in flat end user charges beginning in 1990.

Under this approach, the $4.00 residential flat charge in effect in 1986 could be increased during the last three years of the transition. Using 1984 estimated costs, we estimate that the flat charge for residential lines will average $4.35 for 1987, $4.70 for 1988, $5.05 for 1989, and $5.42 for 1990. The $5.42 figure is derived by dividing the estimated total common line revenue requirement for 1984 (approximately $6.5 billion) by the total number of access lines (approximately 100 million), and dividing the result by 12. It should be noted that this is an average estimated monthly rate; the actual rate could be lower or higher depending upon each telephone company's revenue requirements. After the transition, residential and business end users served by the same company will pay the same interstate access charge per line. The High Cost Factor recommended by the Joint Board in CC

Docket No. 80-286 provides that no end user may be required to pay an access charge which exceeds 200 percent of the national average.

Second, certain remarks made by Chairman Fowler in response to questions posed by Senator Danforth warrant elaboration. It is necessary to point out that, when Chairman Fowler indicated to Senator Danforth that the Commission's flat end user access charges would account for approximately 50 percent of the rate increases which the residential telephone customer could expect by the end of 1986, Chairman Fowler's assumption was that the overall local rates would rise to an average level of approximately $18 by the end of that year. If local rates were to rise above an average of $18—for reasons which have no relationship to the Commission's access charges—then the access charges obviously would account for a smaller percentage of these total increases in local rates since the access charges are held constant at $2.00 for 1984, $3.00 for 1985, and $4.00 for 1986.

In Texas, for example, Southwestern Bell has requested a rate increase which would raise rates for basic monthly service from $10 to $30.35—an increase of 204 percent. If this were allowed to become effective, the Commission's access charge would add $2.00 to this monthly bill in 1984. This would account for only 9 percent of what the total increase may be, or 6 percent of what the total monthly charge in Texas may be. Another example is offered by New Mexico, where Mountain Bell is seeking to raise basic monthly rates from $11.57 to $35.83—an increase of 210 percent. The Commission's $2.00 access charge in 1984 would account for only 8 percent of what the total increase may be in New Mexico, or 5 percent of what the total monthly charge may be.

I hope that this discussion has clarified the remarks made by Chairman Fowler at your hearings, and that it will give the Committees a better understanding of the access charge calculation methods and the relationship between these charges and overall local rates. I would like to request that, if it is possible and deemed appropriate, this correspondence be included as part of the hearing record as an amplification of the remarks made by Chairman Fowler. If I can be of further assistance in providing information regarding the access charge decision, please do not hesitate to call upon me.

Sincerely,

JACK D. SMITH,
Chief, Common Carrier Bureau.

Chairman PACKWOOD. Mr. Chairman, I think we had better conclude this, and we will take about a 10-minute recess and come back at 12:25.

[Recess.]

Chairman PACKWOOD. The hearings will come back to order, please.

We will now move on to our first panel, and I indicate again, it is Chairman Dingell's and my intention to simply go right through until we finish the three panels. So if we could have the panel of the public utilities commissioners: Edward Hipp, Eric Schneidewind, Susan Leisner, and Lisa Rudd.

You have all been very, very patient this morning and we appreciate it. Why do we not start off in the order you appear on our witness list, unless you have arranged the order differently among yourselves. Commissioner Hipp, go right ahead.

STATEMENTS OF EDWARD HIPP, COMMISSIONER, NORTH CAROLINA PUBLIC UTILITIES COMMISSION; ERIC SCHNEIDEWIND, CHAIRMAN, MICHIGAN PUBLIC UTILITIES COMMISSION; SUSAN LEISNER, COMMISSIONER, FLORIDA PUBLIC UTILITIES COMMISSION; AND LISA RUDD, COMMISSIONER OF ADMINISTRATION, DEPARTMENT OF ADMINISTRATION, STATE OF ALASKA, ACCOMPANIED BY JULIANA GUY, DEPUTY COMMISSIONER FOR TELECOMMUNICATIONS

Mr. HIPP. Mr. Chairman and members of both the Senate and House committees: My name is Edward Hipp. I am a member of the North Carolina Public Utilities Commission. I am appearing here also as the chairman of the NARUC's Communications Committee. That committee met yesterday and discussed both of these bills, and then reported to the executive committee of the NARUC yesterday afternoon.

Chairman Packwood. Hold on just a moment.

Could you keep that door going to the outside closed, please.

Go right ahead.

Mr. Hipp. The National Association of Regulatory Utility Commissioners, through their communications committee and through their executive committee also, wholeheartedly support the philosophy of both of the bills that are being considered here today.

The primary reason is the turmoil that we see coming in telecommunications regulation, which will come close to being a crisis if it goes on without any abatement or without any change, because we feel that the burdens being placed upon a substantial number of users by the rate increases threatened by the deregulation changes will be too great.

We appreciate the role the Congress is taking here and the hearings that are being conducted here today, because we think that this is the only way that the problem can be solved. We think that universal service is in true jeopardy under the rate increases that are proposed. There is no question in our mind that the rate increases will average at least 100 percent across the country from the access charges alone, when you consider the interstate access charge and the intrastate access charge together.

Chairman Packwood. Say that again?

Mr. Hipp. We consider that the rate increases on the average customer's bill will be at least 100 percent from the access charges alone, and that is the interstate access charge and the intrastate access charge together. That is the $7 interstate access charge and an intrastate access charge that will probably run $6.

Chairman Packwood. So you mean 100 percent would be over this 3-year period of the phase-in?

Mr. Hipp. It will be over the 6 years, Mr. Chairman. But they are not the only increases that are coming from deregulation.

We have the rapid increase in the rate of depreciation caused by new technologies that is aging out most of the present plant over a very rapid period of time, and because of the competition that is shifting the cost burden from some groups to other groups, primarily from the business groups to the residential groups, to meet the competition in the business sector. And all of those are contributing to increases which will substantially be above those attributed just to the access charge.

So, we think, Mr. Chairman, that the dream that has been expressed some several years, that technology and competition would bring great progress to all telephone users in the United States, is not being met for a major sector of the telephone users, and that is the low- and middle-income sector. And it would be at least 50 percent of the users that are not experiencing the benefits promised by technology and the benefits promised from competition, because of the rate increases that are being imposed upon them.

The new round of rate increases in North Carolina, a 60-percent increase pending by Southern Bell on residential users, which is on residential users almost exclusively and the business users in some of the tariffs are getting an actual decrease and in the overall tariffs to some customers increases of 3 and 4 percent.

These access charges shift such a tremendous amount of the cost from the business sector that was using a large part of the toll, down to the end user that the access charge is the greatest burden that is being placed from all of the changes.

Because of these changes—we have been through both of the major bills that are here, Senator Packwood's bill and Representative Dingell's and Wirth's bill. And we support all of the main purposes and all of the main philosophies of those bills.

We support particularly even the name of the bill, to start with, the Universal Telephone Service Preservation Act of 1983. We think it is well named and needs to be enacted to preserve universal service. We certainly support the purpose, to preserve nationwide availability of basic local telephone service to residential and rural customers at reasonable rates.

And we would urge, finally, if I may conclude, that you persist with the philosophy behind these bills. We have very minor changes that 100 percent of all States may not support in one or the other of the bills 100 percent with all States. There are some differences in the way that a high cost factor might apply, whether it be at 110 percent or 115 percent. There are some small differences over the way a lifeline tariff might be applied or might be provided in national legislation.

There are some small differences about the way the joint board might be structured. The States, of course, prefer a very structured independent joint board, with a strong representation from the States.

The one thing that we do request be changed, in the Senate bill particularly, as distinguished from the House bill, is the provision in the Senate bill that would take away the State jurisdiction over intrastate toll and transfer that to the FCC. We feel like that is more procedural than dealing with the merits, because we do not feel that is necessary to the philosophy of the bills, we believe that the States can retain intrastate toll and still accomplish the purposes of the bill. It is the one main resource that the States have left to try to temper some of the rate increases on local customers.

So with those very minor differences that we have among the States, we certainly support wholeheartedly the philosophy of the bills, and we thank you for this opportunity to make that presentation.

[The statement follows:]

STATEMENT OF THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

Good morning, Mr. Chairman, my name is Edward B. Hipp. I am a Commissioner of the North Carolina Utilities Commission, a position I have held since 1977. I am testifying today on behalf of the National Association of Regulatory Utility Commissioners (NARUC), whose Committee on Communications I chair. Accompanying me today is Rita A. Barmann, NARUC Director of Congressional Relations.

The NARUC is a quasi-governmental, non-profit organization founded in 1889. Within our membership are the governmental agencies of the fifty States, the District of Columbia, Puerto Rico and the Virgin Islands which are engaged in the regulation of utilities and carriers. Our chief objective is to serve the consumer interest by seeking to improve the quality and effectiveness of government regulation in America.

At the outset, I would like to commend Senator Packwood, Representatives Dingell and Wirth, and the members of both the Senate Committee on Commerce, Science and Transportation Committee and the House Energy and Commerce Committee for choosing to move expeditiously on legislation designed to preserve universally available basic telephone service in the United States. That you have convened these unusual joint hearings is an impressive illustration of the high priority you have placed on this legislative effort. Maintaining affordable telephone service for all has long been one of the chief concerns of State utility regulators nationwide. The members of the NARUC are pleased to be in the position of offering you guidance as you seek an appropriate means of ameliorating local rate increases that threaten universal service, rather than one of convincing you and your colleagues that congressional action is indeed needed in this area.

My comments today will focus on the concepts underlying the major proposals before your committees and the extent to which our Association believes these solutions would be effective remedies to the local telephone rate increase problem about which there is such widespread agreement. Two preliminary observations are in order before I turn to that analysis. First, I would emphasize that our objective should be not only prevention of local rate increases that are much higher in some parts of the country than in others, but also prevention of nationwide rate hikes which would be uniformly devastating. Secondly, it is incumbent upon Congress to recognize the crucial role that State regulators necessarily play in assuring the availability of reasonably priced telephone service, and to craft legislative cures which preserve the State's regulatory authority in this regard. Thus we applaud the acknowledgment in the purpose of H.R. 3621 (the Wirth-Dingell bill) that continued universal service depends upon the sufficiency of State regulatory authority.[1]

ACCESS CHARGES

The thrust of virtually all the relevant legislation before you is to set in place a mechanism by which exchange carriers compensated for providing access to the local exchange network. Currently, the long-distance carriers provide such a revenue contribution through the separations process. As a result of the Federal Communications Commission's (FCC's) recent Third Report and Order in its *MTS and WATS Market Structure Inquiry*[2] the burden of a substantial portion of exchange carriers' fixed plant (non-traffic sensitive or NTS) costs is to be shifted to the residential and commercial subscriber through the imposition of end-user access charges. The FCC's chief rationale for mandating this shift is to eliminate disparities in the pricing of interstate toll service attributable to usage-based allocation of NTS costs.

Although the FCC's access charge decision contains the Commission's first explicit acknowledgement that preservation of universal telephone service is required by the Communications Act of 1934,[3] its decision does not otherwise reflect, our view, an appreciation of how universal service will be threatened by the imposition of flat-rate, end-user access charges. Moreover, the Commission has clearly overstepped the bounds of its jurisdictional authority over interstate communications in mandating what is in essence a local service charge. The NARUC continues to assert these arguments in seeking judicial review and reversal of the access charge decision;[4] there is little question, however, that congressional action to redirect Federal policy in this area is a far preferable route. To that end, therefore, we support the intent of both H.R. 3621 and S. 1660 as both measures relate to the establishment of an access charge mechanism.

Regarding the specifics involved in establishing and implementing an access charge system, the NARUC believes that both responsibilities should be delegated to the State commissions insofar as possible, in accordance with flexible Federal guidelines. The Wirth-Dingell bill would require only partial FCC delegation of such authority (that relating to access tariffs for interexchange carriers that directly interconnect with exchange carrier facilities[5]); it would give the FCC exclusive authority over access charges for indirectly interconnected carriers and for carriers which offer alternative exchange access facilities or services comparable to those offered by exchange carriers.

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[1] *See* Section 2(b)(3) of H.R. 3621; *see also* Section 2(b)(3) of H.R. 3440, a bill proposing the Universal Telephone Service and Ratepayer Protection Act of 1983.

[2] CC Docket No. 78-72 (released February 28, 1983).

[3] Third Report and Order, pp. 27-29.

[4] See brief of the NARUC in *NARUC* v. *FCC and USA, et al.*, Docket No. 83-1225, United States Court of Appeals for the District of Columbia.

[5] See proposed Section 221(c)(9)(A) of H.R. 3621.

Moreover, even this partial delegation is further weakened because it would be subject to FCC rules or procedures as well as to FCC review. S. 1660, on the other hand, would vest exclusive authority over access charges with the FCC and permit the Commission to decide whether and to what extent such authority should be delegated to the State commissions.[6]

Although the approach taken in H.R. 3621 is preferable to that contained in the Packwood measure, we feel strongly that neither bill proposes a satisfactory jurisdictional division of responsibilities with respect to access charges. Furthermore, provisions in both bills should be revised so as to maintain the maximum degree of flexibility practicable in the computation and imposition of access charges. Specifically, the NARUC believes that the legislation should not preclude State regulators from considering non-cost-based factors, such as value of service, for example, in formulating interstate access charges. State regulators should be free as well to adopt access charges which have (*or* have not) an end-user fee component.[7]

Implicit in our view that the State commissions are the appropriate authorities to oversee the creation and maintenance of an interstate access charge system is our vigorous support for a continuation of the jurisdictional allocation of regulatory authority provided for in the 1934 Communications Act. The State commissions are clearly the most desirable forums for the resolution of issues which directly impact upon local telephone rates. Where matters of joint concern are involved, use of the Federal-State Joint Board mechanism is appropriate. We therefore strongly oppose that provision of S. 1660 [8] which would allow the FCC to assert jurisdiction over all NTS subscriber loop costs attributed to the Federal jurisdiction.

UNIVERSAL SERVICE FUND

Turning to the Universal Service Fund mechanism, the NARUC supports establishment of such a means of assuring that universal telephone service is available at affordable rates throughout the Nation, including, but not limited to, rural and remote areas. (H.R. 3621's proposed Section 225(a) employs language which closely tracks the State regulatory position on this question.) The Packwood and Wirth-Dingell measures propose two distinct formulas for exchange carrier eligibility for subsidies from the USF. The NARUC is still studying the ramifications of these formulas and thus takes no position favoring one over the other at this time.

As I mentioned earlier, the spectre of local rate increases that are precipitous yet applicable across-the-board is just as alarming to State regulators as is the prospect of increases which are much higher in some areas than in others. Given the fact that the USF proposed in most of the legislation before you would be designed to remedy only deviations from the nationwide average cost of local service, a transitional mechanism, such as the transitional account proposed in Section 225 of the Wirth-Dingell bill, is essential. The NARUC thus advocates making this transitional account a permanent mechanism, so as to assure a minimum level of revenues for exchange carriers (i.e., that received in 1982) as the move to the access charge system is made.

Regarding penalties for violation of the proposed Federal statute, the NARUC prefers the $100,000 level contained in S. 1660 rather than H.R. 3621's $50,000 level, for the obvious reason that potential bypassers could absorb the latter fine more easily than a $100,000 penalty. However, we request that S. 1660's standard for imposing such a penalty—avoiding access charge payments with the intent to deprive an exchange carrier of revenues—be revised so as to be less restrictive. In light of the unprecedented character of the access charge system, proof of such "intent to deprive" is an unreasonably stringent burden.

Regarding proposed guidelines for payments from the USF contained in H.R. 3621, we suggest that the last of these criteria may well be inconsistent with the legislation's intent to protect universal telephone service. This provision would condition USF payments on whether they "unreasonably impede the entry and operation of competitive suppliers of exchange services,"[9] It would be premature to enact such a requirement absent a thorough analysis of whether unbridled competition at the local exchange level is in the public interest.

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[6] See proposed Section 221(g) of S. 1660.

[7] Proposed Section 201(f) of S. 1660 would completely preclude imposition of end-user charges.

[8] See proposed Section 221(f).

[9] See proposed Section 225(d)(2)(D) of H.R. 3621.

UNIVERSAL SERVICE BOARD

The successful implementation of the USF depends largely on the administration of the Fund provided by the Universal Service Board as proposed in the universal service legislation. The NARUC believes it is essential to the effective administration of the USF that the overseeing body be composed of a majority of State commissioners and that it be granted administratively final authority. Our long experience with the current Joint Board mechanism, under which the FCC must refer separations matters to a State-majority Joint Board for an advisory decision,[10] has demonstrated that effective State input in the decision-making process depends upon more than majority representation on the Board. The expertise of the States will be invaluable in ascertaining exchange carriers' revenue requirements and consequent eligibility for USF monies. The FCC should not be given the power to alter the determinations of a body whose composition accurately reflects the States' closer vantage point in this regard. We therefore endorse those provisions of H.R. 3440 which would establish a Universal Service Board composed of three State commissioners and two FCC commissioners and empowered to make administratively final decisions.[11]

In addition, we request that language be added to any resulting legislation which would authorize payment of travel expenses for the State members of the Universal Service Board and their State staff members.

PREEMPTION OF STATE AUTHORITY OVER INTRASTATE TOLL RATES AND SERVICES

S. 1660 would transfer to the FCC existing State regulatory authority over intrastate interexchange rates and services.[12] The NARUC submits that such a jurisdictional transfer is not merely an unnecessary facet of universal service legislation; it is rather a proposal that would only exacerbate the problem of local rate increases that the legislation is intended to remedy. Preemption of State authority over intrastate toll services would require that the FCC's judgment be substituted for that of the individual State commissions concerning issues that are purely intrastate in nature. Apart from the fact that this sharply conflicts with the basic principles underlying our Federalist System, it would further reduce the panoply of regulatory tools currently at the States' disposal to ensure fair rate structures which promote universal service within their respective jurisdictions.

This is exactly the wrong direction that congressional action in the telecommunications policy area should be taking at this time. Stripping the States of their intrastate toll jurisdiction would serve no purpose other than to usurp legitimate State authority and make the critical task of maintaining reasonable telephone rates even more difficult.

We therefore request that no such provision be included in any resulting legislation.

OTHER ISSUES

In the interest of time and succinctness, I will make only brief comments on other significant issues raised in the major bills. We would be pleased to provide your committees with more elaborate explanations of our positions on these matters at a later date.

DEPRECIATION

The NARUC strongly supports Section 7 of H.R. 3621, which would clarify State authority over depreciation methodologies for exchange facilities and for the portion of jointly used facilities assigned to the States' jurisdiction by the proposed Universal Service Board. The FCC's recent decision to preempt such State authority is one of a number which, if left intact, will exert yet more upward pressure on local telephone rates.

PROVIDER OF LAST RESORT

Likewise, State regulators support proposed Section 227 of the Wirth-Dingell bill, which would permit State commissions to require exchange carriers to provide and maintain basic telephone equipment upon customer request. This provision parallels a recent FCC decision adopting a modified version of the NARUC's provider-of-last-resort proposal. Assuring that basic equipment is obtainable for every telephone subscriber is clearly in line with the goal of making basic service universally available and affordable.

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[10] See 47 U.S.C. § 410(c).

[11] See proposed Section 227 of H.R. 3440.

[12] See Section 5(a)-(c) of S. 1660.

LIFELINE SERVICE

The NARUC supports Federal legislation enabling the FCC and the State commissions to make "lifeline" telephone service available at discounted rates, if deemed appropriate by such regulatory authorities.

CROSS-SUBSIDIZATION PROHIBITION

The NARUC submits that consideration of revenues from certain unregulated services or products other than from printed directory advertising, or Yellow Pages, should be permitted in determining exchange carriers' revenue requirements. Specifically, we suggest that revenues from cellular services and from the sale of new customer premises equipment be permitted to be so considered.

CONCLUSION

Mr. Chairman, I would like to reiterate our unqualified support for the congressional effort to preserve universal telephone service in America. Your deliberations on this matter are more than timely: they are an essential precondition to a speedy resolution of the local rate increase dilemma that faces us all. The members of the NARUC stand ready to assist you as you seek such a resolution.

Thank you for your attention.

Chairman **PACKWOOD**. Commissioner, thank you.

I think you addressed your comments very appropriately, because it is a philosophical issue and for those who do not agree with the philosophy of the bill there is not much we could do to change it that would make it satisfactory. For those that do agree with it, I am convinced the differences can be harmonized.

Commissioner—do I pronounce it correctly—Schneidewind?

Mr. **SCHNEIDEWIND**. That is absolutely perfect.

Senator Packwood, Chairman Dingell, Senators and Congressmen, all of us are here today, I think, because we recognize that the telephone consumers of the United States are going to get hit with a sledge hammer in the next 12 months, and after that it is only going to get worse. That sledge hammer is not being driven by just a little old $2 access charge. It is the cumulative result of a number of decisions that have been taken.

The FCC's access charge will be a major factor in rate increases. The FCC's preemption of State depreciation practices will be almost as great a factor, and takes away from us the authority to set capital recovery rates, and it will have a tremendous increased impact on rates.

In addition, the breakup of the AT&T system takes away from the Bell operating companies a large and profitable segment of their intrastate long-distance business, and those profits will have to be made up in the form of local increases or else we will see deterioration of the phone system.

Finally, the entire system of revenues and business in the telephone industry has been changed. It is now a funnel in which costs come in from many different areas and come right down on the local service rate, without the ability to spread those costs, as we did in the past, over equipment, long distance, and local services. Now they all come down on local services.

So why are we here? It is not because of a little $2 access charge that will grow and grow. It is because of many factors that came together.

But that is not really the reason that we are here. We are here because many policymakers in many different areas of regulation did not have before them a clear, precise, and legally binding standard which would have made their actions march to the tune of universal service. They had no requirement binding upon them to tailor their actions to the requirement that service be affordable. Rather, they acted independently and let the results come together in what I think is a haphazard manner, in a manner that Congress is now finding that it cannot live with.

So what are we going to do, to urge you to do today? It is not to create a new system, without caution and without due process, look at a new system. It is to start the process of saving an existing system that has worked well in preventing a catastrophe. That is what we are here to do today.

And we are here to talk about a transition to a new system which will combine competition and universal service, but will do it in a way that is measured and deliberate and is based on fact rather than being done in a haphazard fashion, which has come together in a way that none of us can live with.

What is that new policy that we are looking for, at least at the State level? First and foremost—and it is the one point that I would stress above all other points, and that is that there must be a linchpin, a keystone, a foundation to that new piece of legislation, and that must be the notion that the existing penetration of telephone service into this Nation must be preserved. It must not be allowed to erode.

That policy must be expressed in such clear terms that subsequent decisions of regulatory bodies and other bodies, which you cannot specify in any piece of legislation, will be guided by and in fact required to comply with such a requirement. So the requirement must be in there that will provide the guidance in a legally enforceable standard of universal service which can be used to test any of the innumerable actions which will take place in the years to come in various regulatory agencies.

The second linchpin of the strategy, narrowing down, is a standard or law that will allow all telecommunications users to contribute to a system when it is necessary to preserve the system, to treat our telecommunications system like a system of fire protection, police protection or schools, which cannot survive if people may opt in and out at will. For in such a system the strong and the wealthy will always have the services they require, but the service for the low-income people, for the rural user, will deteriorate and disappear in many instances.

So there needs to be a funding mechanism which will support the system for all.

Third, there must be participation by State regulators and Federal regulators in policysetting on both access charge mechanisms and depreciation, to set some national sense of direction, but leaving implementation of the specifics at the local level in both those critical areas, so that we can tailor cash flow and the amount of basic rate increases to local conditions.

Finally, the last element of a policy must be that consumers who require, and indeed have no choice but to require, the installation and maintenance of a basic instrument from some entity, have that at their disposal, and that State regulators have the authority to require a basic instrument to be installed and maintained where necessary and where alternate providers do not exist.

Mr. Chairmen, both Chairman Dingell and Chairman Packwood, that is an outline of the broad policy of telecommunications which indeed could combine competition and universal service, and is broad enough to survive the decades to come. We ask for your help in working for such a policy.

Thank you.

[The statement follows:]

STATEMENT OF ERIC J. SCHNEIDEWIND, CHAIRMAN, MICHIGAN PUBLIC SERVICE COMMISSION

Chairman Packwood, Chariman Dingell, Chairman Wirth and members of the Senate Commerce, Science and Transportation and House Energy and Commerce Committees.

For the last year and a half, state regulators have warned that local telephone exchange rates were going to double or triple as a result of pending federal actions. State regulators listed the proposed Modification of Final Judgment, the preemption of depreciation practices by the FCC, the implementation of Computer II, and finally the access charge order (CC Docket 78-72) of the FCC as the causes of the doubling or tripling of local exchange rates. Let us review events which have occurred since our first warning.

State regulators have participated vigorously in the proceedings before Judge Harold Greene and have managed to reduce the adverse impact of the Modification of Final Judgment on local exchange rates. The proposed Modification has been altered to allow the Yellow Pages operation to remain with operating companies, to allow operating companies to reenter the customer premises equipment market and other markets at the option of Judge Greene, and the operating companies have been granted significant revenues from patents and licenses filed by AT&T, as well as use of the Bell logo and trademark. Finally, we have obtained assurances that the costs related to network reconfiguration and additional equipment to assure equal access, which were caused by divestiture, would be borne by AT&T or other interexchange carriers. These alterations in the proposed modification of Final Judgment have enhanced the economic future of the Bell Operating Companies, as well as having a favorable impact on the cost of local service.

Unfortunately, the fact remains that the massive administrative costs of divestiture, costs of network reconfiguration and equal access which are incurred, but not as a result of divestiture, as well as the loss of the most profitable intrastate toll revenues to AT&T, will result in significant rate increase for the local customers of Bell Operating Companies throughout the United States. In Michigan these increases were originally estimated to be $3.00 per customer per month, but will be somewhat reduced if AT&T and the Department of Justice fail in their attempt to obtain reconsideration or reversal of Judge Green's decision to impose divestiture-related equal access on AT&T.

In addition, the FCC has preempted the states' depreciation authority and at the same time ordered implementation of new depreciation methodologies which will assure more rapid capital recovery and, hence, higher local rates for many local exchange customers.

In Michigan, the ultimate effect of this FCC order will be about $2.55 per customer per month if the position advocated by FCC staff for implementation of CC Docket 79-105 is adopted. Implementation of the FCC staff position was averted, at least until 1984, be settlement of a pending Michigan Bell rate request (U-7473), which specified a compromise means of retiring reserve deficiencies related to adoption of remaining life by amortizing such deficiencies over 10 years. Use of this compromise enabled the Michigan Commission to adopt the Remaining Life concept while approving increases equivalent to only about $1.25 per month, rather than the $2.55 per month inherent in the FCC staff position. If states such as Michigan fail in their court challenge of CC Docket 79-105, which preempted state authority over depreciation practices, the FCC can be expected to require depreciation practices which raise telephone rates in Michigan by about $2.55 per month above levels in effect January 1, 1983.

All states are facing a January 1, 1984 implementation of the FCC's access charge order and indications are that, if anything, exchange carriers will be requesting higher interstate flat fees in their access charge mechanisms than had ever been anticipated. Our original estimate was that interstate and intrastate access charges placed directly on the customer would total $4 per month in Michigan. While the relationship of the level of interstate to intrastate access charge has not been determined, the total of both charges requested by Michigan Bell will undoubtedly equal or exceed $4 per residential customer per month unless the FCC reconsiders its decision.

Another decision in FCC's Docket No. 79-105 required exchange carriers to expense, rather than to capitalize, the costs related to station connections. This change in accounting treatment began in 1981 and will be fully applicable by 1984, adding approximately 60¢ per month per customer to the bills of Michigan basic telephone service customers.

Also, the FCC issued an order in CC Docket No. 80-286, which will phase out the toll support for existing leased terminal equipment by year end 1987. This order will add approximately 63¢ per month per customer to the bill of a basic telephone service subscriber by 1984. Further rate increases will be required as a result of the subsequent portions of this phase-out.

The Modification of Final Judgement proposed on January 8, 1982 by the Department of Justice and AT&T will have a severe impact on the cost of service for the basic telephone serice subscriber. The first detrimental impact will occur because, taken together with the FCC's Computer II decision, the Modification of Final Judgement destroys the ability of state regulators to spread the costs of basic service over various optional equipment offerings and intrastate toll service which are, in most cases, purchases made at the option of a customer. The Modification of Final Judgement requires the Bell Operating Companies to spin off inter-exchange intrastate toll services and transfer this business to AT&T. This organizational change will make it impossible for state regulators to use profit from long-haul intrastate toll to support basic service or to spread revenue requirements from basic service offerings onto toll offerings. Thus, increased expenses in the telephone exchange will be placed on the basic telephone rate because such expenses cannot be added to toll, equipment or other non-basic services.

In summary, then, state regulators in general, and those of us in Michigan in particular, must view the future of exchange service with a great deal of alarm when we realize that the cumulative impact of the federal actions described above will be to approximately double basic telephone service in Michigan within the next twelve months and to cause even higher rate increases in other states.

It has been widely acknowledged that sudden and significant increases in telephone rates will cause many customers to discontinue basic telephone service. Several estimates have been produced which attempt to quantify the percentage of customers who discontinue telephone service as the result of any given level of increase. The most recent review of this subject is contained in Appendix G of the FCC's access charge decision, CC Docket No. 78-72, dated December 22, 1982. This Appendix, at paragraph 4, indicates that "Most of the Measures" of price elasticity "fall around −.1; that is, a 10 percent increase in price will lead only "a 1 percent decrease in the quantity purchased." In other words, the FCC conclusion is that a price increase for basic telephone service customers of 100 percent will cause 10 percent of these customers to drop their basic telephone service.

In Michigan, a bit of recent history would lead to the conclusion that the FCC estimate is on the conservative side. In 1975, the Michigan Public Service Commission issued an order increasing the rates of the Hickory Telephone Company by 54 percent from $10.66 to $16.35. As a result of this increase and a significant amount of local concern, approximately 14 percent of the customers discontinued their basic telephone service.

It is safe to predict that a sudden doubling of telephone costs to basic telephone service customers will cause at least 10 percent to 14 percent of these customers to drop basic telephone service, but, unfortunately, the drop-off will not stop at this point. Once customers discontinue their telephone service and cease paying on a regular basis, the costs of the plant that was installed to serve them must still be paid. Unfortunately, as with the railroads during the fifties and sixties, the reaction of a regulated utility to the loss of customers is to request and generally obtain the right to spread its existing fixed costs over the reduced number of customers still remaining on the system. This can produce a deadly spiral in which revenues go down through loss of customers, fixed costs are spread over fewer customers, which in turn causes rate increases to those customers and a further loss of customers.

Let us follow this process through several cycles. If Michigan Bell loses 10 percent of their customers, the necessity of spreading those fixed costs over the remaining customers would cause a rate increase of 11 percent to the remaining basic service customers. If 14 percent of their basic service customers discontinue service, the impact would be a 16 percent rate increase for the remaining customers. These increases, using the price elasticity data above, would cause a further drop-off of 1.1 percent of customers in case of the 10 percent drop-off or 2.2 percent of customers in the case of the 14 percent drop-off.

If we follow this process through one more cycle, the result would be a third loss of customers of .1 percent in case of the 10 percent drop-off and .3 percent in the case of the 14 percent drop-off. Thus, in total, a doubling of rates could cause a cumulative drop-off of 11.2 percent if our price elasticity data is −.1 and 16.5 percent if our elasticity figure is −.14. In other words, a doubling in basic service rates could cause a cumulative loss of basic telephone service to one out of every 9 customers or one out of every 6 customers.

It is quite likely that many states will see a tripling of basic telephone service costs, rather than a doubling, and in these states, it is quite possible that one out of every 4 customers could lose basic telephone service.

It is my contention that a loss of basic telephone service in the magnitude described above will destroy the concept of universal telephone service in this country.

In economic cost, citizens in rural or inner city areas would immediately experience higher insurance costs due to a lack of rapid access to fire protection, and could experience similar increases in health insurance costs due to a lack of emergency access to health services.

It will no longer be possible for these citizens to obtain rapid access to home repair services, banking services or other retail services, including receipt of calls placed through the telecommunications services provided by competitive Other Common Carriers. Businesses in these areas will obviously suffer indirectly from this lack of access. In the larger context, both business and government will suffer if 1 out of every 9 or 1 out of every 6 families does not have access to a telephone. Large industrial or retail corporations will find that many of their workers cannot call in sick and arrange for substitute employees. Similarly, corporations or government agencies will find that they cannot quickly communicate with all of their employees in the event that a plant is shut down for emergencies or other technical reasons. Much governmental planning for emergencies depends upon the ability to communicate by telephone with literally all citizens. In the case of natural disasters, such as floods, tornadoes or chemical spills, no assured, alternative means of communication really exists. Military preparedness could similarly suffer from the lack of ability to quickly and surely contact reserve personnel for call up to duty. The banking institutions which have depended upon the telecommunications network as a future means of making banking services available quickly and rapidly to rural or elderly customers will have to modify their plans.

The existence of universal telephone service has made it possible for people in rural areas and in inner city areas to become part of the national telecommunications network of the future. Suburban areas which are populated by people with access to surface transportation or nearby commercial institutions will find alternative means of conducting their business or obtaining emergency services. It is the rural and inner city areas that do not have access in many cases to alternative forms of transportation because of their widely dispersed geographical nature or because of income limitations that prevent purchase of automobiles or maintenance of these vehicles. The loss of universal telephone service, therefore, could make large rural areas and inner city areas virtually off limits for much of the business and governmental activity that goes on today and is planned for the future.

In addition, the absence of basic telephone service could subject inhabitants of rural areas or inner city residences to far higher costs of insurance or health care services than would currently be the case. Businesses which now can quickly and efficently access the residences of rural and inner city areas will find that in many cases they do not have economically attractive alternatives to the telephone for reaching these people. In effect, the loss of universal telephone service could make large areas of our country off limits to business and government.

The break-up of the AT&T system, as well as recent actions of the FCC, have combined to force the United States Congress to make a historic decision. This decision will determine the fate of the telecommunications system in the United States for decades to come. At first glance, it appears as though Congress is being asked to choose between benefits of competition and the benefits of universal service. On the one hand, the concept of universal service has served this country well and given it a communications system unmatched around the world, a high quality communications system which serves about 95 percent of our people. On the other hand, the benefits of competition promise to make available new equipment and new services in unmatched variety and at lower price potentially than under any other economic system.

I am one who calls on Congress to forge a bold new telecommunications policy which will combine the benefits of competition and universal service for the decades to come. I call upon Congress to make the clear commitment to a uniquely American communications policy which will harness the benefits of competition where competition has been proven an effective delivery mechanism for goods and services and to make the decisions necessary to preserve a system of universal service that has served this country well for fifty years.

The new telecommunications policy set forth by Congress must prevent the wholesale bypass of local exchange telecommunications systems, recognizing that bypass of those systems will be a financial catastrophe that would eliminate the ability to provide high quality, pervasive telecommunications services. At the same, the new telecommunications policy must avoid concentrating the cost of the telecommunications system on the basic customer and, thus, promoting the large-scale drop-off of lower income Americans.

The new telecommunications policy forged by Congress must ensure that Americans will have access to the widest variety of competitively priced equipment that the world's markets can offer, as well as access to many different companies that provide innovative transmission services for voice, data and uses undreamed of today. But at the same time, this new telecommunications policy must assure that all Americans have the opportunity to the connected by a viable and technically advanced system which will serve their basic needs and enhance the economic future of this nation as a whole.

What are the steps necessary to achieve this bold new telecommunications policy?

First, the new policy of telecommunications must recognize that the heart of our telecommunications system is the local telecommunications exchange. Without sound physical plant and universal access at the local level, no telecommunications network can truly be universal, pervasive, or an asset to our nation's economic future. No telecommunications system can serve to unite Americans at a national or state level unless the local plant and personnel are of the highest quality.

Second, the new telecommunications policy must recognize that a sound, reliable and advanced local telecommunications system cannot exist if such a system is supported by only a few low-income or low-volume customers. It goes without saying that recent advances in the cable industry and the penetration of cable systems throughout the United States, as well as other technologies, have created competing networks at the local exchange level. Congress must face in a forthright manner the question of whether more than one basic telecommunications network can be financially sound at the local level. If some sense of order is not brought to the potential chaos of numerous local communications networks serving the local community, none of these networks can prosper serving the needs of the basic services customer and in all likelihood, the local telecommunications system will wither and die.

This leads unavoidably to the conclusion that the government has a role to perform in ensuring that at least one comprehensive, universally available local exchange network is available to serve each and every American. Such a universally available network cannot exist any more than a fire department, police department or school system can exist if there is not some universal obligation to support such a system. It is truly a legitimate role of government to make sure that basic services necessary to the welfare of the community are supported by all, rather than a few. For if only the few support a basic service, the service will either become prohibitively expensive or its quality will deteriorate through lack of funding. The required level of funding need not be limitless, but it must be of an amount which will ensure that the current penetration of telephone service on a national level is not reduced. This test, and only this test, is legitimate as a goal and basic principle for our national telecommunications policy.

In practical terms, this means that all providers of telecommunications service, whether public or private, have a basic obligation to support the local exchange network at a level necessary to bridge the gap between the revenues that may be collected without driving customers off the system and the level of revenues necessary to preserve, maintain and upgrade a local telecommunications network that is available to all and useful to all.

The second basic principle of a telecommunications policy must be to allow responsible local authorities the full latitude necessary to discharge their telecommunications responsibilities. Specifically, this means that the preemption by the FCC, in its Order 79-105 of state PUC depreciation authority over local telecommunications plant, must be repealed. State regulators are rightfully held responsible for the quality and availability of exchange telecommunications service at the local level. Yet, it is impossible, or will be impossible, for them to discharge this responsibility if so basic a component of ratemaking and telecommunications utility health as depreciation is exercised by a body in Washington that is not held responsible for rates or quality of service at the local level. Moreover, it will be impossible for any federal authority to actively involve itself in the intricacies of cash flow requirements for thousands of local telecommunications providers. Without the authority to establish depreciation practices for local plant, state regulators in fact will be deprived of the means to discharge their responsibilities to local customers and the federal regulators will not have the familiarity with local conditions necessary to perform their duties in a sensitive and accurate fashion.

This is not to say that overall national goals or policies regarding depreciation practices may not be appropriate. Rather, it may be desirable to establish broad goals through recommendations or policies at a national level but ensure that local state authorities have the flexibilities necessary to tailor those policies to local conditions, revenue requirements or customer needs. An excellent example of this phenomenon occurred in a recent Michigan Bell rate case U-7473, in which the Michigan Public Service Commission approved a settlement which adopted the Remaining Life concept. Instead, however, of disposing of reserve deficiencies in a manner consistent with FCC staff policy, the MPSC approved a ten-year amortization schedule which guaranteed the company recovery of unfunded reserves and at the same time lessened the rate impact that more rapid recovery would have caused. This is an example of a Commission willing to address needs for more rapid capital recovery, but at the same time easing the transition to those new methods in such a way as to preserve universal service. Such flexibility is absolutely imperative to the ability of any local regulator to preserve both quality of service and affordability of service. Thus, national telecommunications policy must reemphasize the role of the local regulator in the depreciation arena while speaking to the need for policies or recommendations at a national level which will assure capital recovery policies that build and maintain a high quality telecommunications network.

In CC Docket 78-72, the FCC implemented an access charge structure which over a period of five years will place an increasingly heavy burden for interexchange access on the local telecommunications customer, whether or not that customer uses interexchange telecommunications services. The placement and amount of that burden by the FCC was done in a fashion which gave the local regulator little ability to avoid large increases in the basic service rate. Other means of addressing a legitimate revenue requirement without charging the interexchange toll system were not permitted to state regulators. Once again, flexibility at the local level might have enabled local commissions to recover the necessary revenue in ways which were both fiscally sound and avoided large-scale rate increases on the basic telephone service cost, which in turn would provoke large drop-off in the telecommunications system. It should be clear by now that many alternatives existed to the flat CALC charge utilized by the FCC. State commissions wishing to exercise such options might have restructured their short-haul toll rates to recover more funds or reconfigured local calling areas to generate more toll revenue, considered various message charges on toll or exchange calls or permitted a more gradual transition to any CALC that may become necessary. These alternatives could generate the revenue necessary to offset reductions in the usage component of access charges. None of these alternatives are easy, yet many of them might have been used to avoid the large increases being placed on low-income and low-toll users.

A new telecommunications policy must contain a framework for setting access charges which allows meaningful participation at both the national and local levels. Such a policy must start revenues at the current levels of support being received through the separations and settlements procedures. Next, a new access charge policy must involve both state regulators and federal regulators in a joint board which will establish access charge policy. This joint board could develop guidelines and rules which were broad enough to ensure that bypass would be avoided at the local level, yet essential revenues generated to support the telecommunications system. At the same time, the joint board should be limited to the role of providing broad guidelines with implementation of these guidelines at a local level being left to state commissioners, or at the option of state commissioners, relinquished back to a federal authority such as the FCC. The new telecommunications access charge policy could provide an avenue of appeal for local commission decisions to the joint board to assure all carriers of fair treatment and the ability to obtain a hearing outside a local jurisdiction.

Finally, a new national telecommunications policy rightfully must rely upon competition as the main source of providing customer premises equipment. This policy would recognize that the competition in the provision of sophisticated business telecommunications equipment has worked largely to the benefit of all customers. Similarly, many residential customers have benefitted in terms of price and choice from competition in the residential customer presmises equipment market. But there are many Americans who are unable to take advantage of a competitive customer premises equipment market. Many of these Americans live in rural areas, low-income urban areas or are physically or mentally disadvantaged. These people will continue to depend upon the local exchange company to provide at least the basic telephone instrument and maintenance of that instrument on a leased basis. It is sound policy to require that at least one provider in each area be available to install and maintain the basic telephone instrument to communicate in this society. Provision of such instruments can be consistent with competition if it is fully compensatory to the local exchange telecommunications company and if state regulators are given the choice of requiring local exchange carriers to provide basic instruments. In this way, state regulators may choose to require a local exchange carrier to provide equipment in areas which are not currently being served and yet may decide that in many areas sufficient competition exists to exempt the local exchange carrier from such a requirement. In any event, the need of society for a reliable, pervasive telecommunications system will be served by ensuring that each resident has access to both the telecommunications system and the basic instrument necessary to access that system.

The four principles listed above would combine to provide a telecommunications system that preserves existing levels and pervasiveness of telecommunications service and at the same time provides competition in the provision of interexchange service and equipment. By requiring all telecommunications users to contribute to the local exchange system, the vitality and technical excellence of that system would be preserved while giving all users the option to use the system or not, at their discretion. At the same time, all Americans would have a choice of customers premises equipment and interexchange services.

This is the time for Congress to plot a course of telecommunications policy for the rest of this century. A wise course will combine competition and universal service and recognize that universal service in telecommunications, as with schools, fire and police protection, may not be maintained without some basic obligation on the part of all Americans to maintain a system that benefits all. This basic decision, coupled with a decision to return to states the level of authority necessary to make the local system responsive to local needs, will create a telecommunications system that can survive any imaginable level of technical change and still provide high quality, universally available service.

Chairman **Packwood**. Thank you.

Commissioner Leisner.

Ms. **Leisner**. Thank you, Mr. Chairman.

Congressmen and Senators, I am very pleased to be here today to comment on the proposed legislation to insure the affordability of local phone service for all Americans.

Not too long ago, last year after the AT&T divestiture was announced, State regulators from across the country tried to assess its impact on local rates. As you may recall, Mr. Brown of AT&T said rates need rise no faster than inflation. Judge Greene concurred and said that rates need not rise because of the Bell breakup.

Then last December the FCC made its access charge decision, switching billions of dollars in costs onto local phone customers. Once again, State regulators tried to assess the impact not only of the divestiture and the access charges, but also of the FCC ruling taking away our jurisdiction over depreciation methodology.

We concluded that a doubling or tripling of rates was soon to be seen in this country. We thought rates of $30 to $35 a month would be here within 1, 2, or 3 years after divestiture.

Well, it turns out we were all wrong. The inflation rate is now hovering around 4 percent, while the rate requests we are seeing are 50 to 250 percent. We are seeing all of the Bell operating companies filing rate requests throughout the country, citing the divestiture as a primary justification for these requests.

And we, the regulators, were also wrong. We were far too optimistic. Those $30 a month rates we were predicting for 1, 2, or 3 years from now are here today in Texas and Tennessee, as you have already heard.

Word of these impending rate increases is finally getting out. It is getting out to local politicians, to the State regulators, who have known about it all along, to Congress, and most importantly to the local ratepayers. It is now time for Congress to act.

First, you must overturn the FCC's access charge decision and prevent those billions of dollars in costs from being shifted onto the local consumer.

Second, you must take care to keep as many people as possible on the telephone network, regardless of where they live and what their income might be. The soul of our society is at stake here. We cannot become a nation divided by technology, where business and the wealthy use their computers, their microwave dishes, and their fiber optic cables, to benefit from the world's most advanced communications network, while an entire underclass exists that does not even have the ability to pick up the receiver on a plain black telephone and dial 911 in an emergency.

We must maintain universal service in this country, and if that means building a universal service fund to provide continued support for this national treasure, then that is what we must do. All providers and all users of the telecommunications network should contribute to that fund, including long-distance carriers, bypassers, and private systems.

It is imperative for the interest groups that are now benefiting so enormously from deregulation, competition, and the AT&T breakup to shoulder some of the burden that these actions are shifting to the local consumer. What we are asking today is that these enterprises give up just a very small part of their not inconsiderable revenues to insure that the American people have the ability to afford basic telephone service, to communicate with their neighbors, their relatives, and their government.

None of us wants to turn the clock back on the great advances we have seen in technology, but neither do we want to return to a time when only a few people had a phone in their homes.

It might be well to remember one of the great political miscalculations in recent history. It occurred in 1936, when the Literary Digest, then the Nation's most popular magazine, did a postcard poll on the upcoming Presidential election. The results of that poll indicated that there would be a landslide victory for candidate Alf Landon.

What did the Literary Digest go on? First, they used the subscription list of their own subscribers, who were much better off than most people in the country. And second, they added to their own list two lists of two other wealthy groups in the country, automobile owners and, you guessed it, telephone subscribers.

It seems that back in the 1930's the vast majority of the American people did not own a telephone. They could not afford a telephone, but they sure could vote.

Let us hope that Congress acts now so that we do not have a recurrence of this phenomenon in the next decade. Thank you.

[The statement follows:]

STATEMENT OF SUSAN W. LEISNER, COMMISSIONER, FLORIDA PUBLIC SERVICE COMMISSION

Congressman and Senators, I am extremely pleased to be here today to comment on proposed legislation that will ensure the affordability of basic telephone service for all Americans.

Not long after the AT&T Divestitute was announced, state regulators from around the country began to assess its impact on local rates. As you may recall, Charles Brown, AT&T Chairman, claimed that rates would rise only as fast as inflation. Judge Harold Green concurred and stated that local rates, indeed, would not have to be raised because of the Bell break-up.

Then, last December, the FCC made its decision to impose long distance access charges, in the form of a flat monthly fee on telephone users, regardless of whether any long distance calls are made. Once again, state regulators tried to assess the impact on local customers. We finally concluded that the combination of the demise of the AT&T monopoly, the FCC's disastrous access charges decision, plus new depreciation and accounting methodologies being forced on state regulators by the FCC would double or triple local rates, forcing a $30 basic monthly residential fee within a short time after divestiture was completed.

Well, it turns out now, that we were all wrong. Inflation is hovering at around 4%, while rate requests are reflecting 50% to 250% increases. Bell Operating Companies are filing rate cases throughout the country claiming divestiture as a primary justification for needed increases in revenues. It appears that even state regulators were overly optimistic in assessing the swiftness and magnitude of these local rate requests. We foresaw $30 to $35 per month rates 1, 2, or 3 years after January 1, 1984. This startling prediction proved to be an underestimation. These dollars increases are today, in rate requests filed recently in Texas and Tennessee.

For awhile, at least, after the death of H.R. 5158 last year at the hands of AT&T, there seemed to be little congressional interest in putting forward any new telecommunication legislation. There appeared to be a "let's wait and see if something terrible happens" attitude. Well now something terrible has happened—recordbreaking rate requests across the country, compounded by an FCC plan to shift some $7 to $9 billion in costs from the long distance market to the local consumer.

The word of these impending rate increases is finally getting out, not just to state regulators, who have known about it from the start, but to local politicians, the Congress, and most importantly, to the ratepayers themselves.

It is now time for Congress to act. First, you must overturn the FCC access charge decision and prevent those billions of dollars in costs from being imposed on all of this country's ratepayers in a flat monthly charge. Secondly, you must take extreme care to keep as many citizens on the telephone network as possible, regardless of where they live and what their income might be. The soul of our society is at stake here. We cannot become a nation divided by technology, where business and the wealthy use their computers, their microwave dishes, and their fiberoptic cables to benefit from the world's most advanced telecommunications network, while an entire under-class exists without even the ability to pick up the receiver on a plain black telephone and dial 911 in an emergency.

We must maintain universal service in this country. And if that means building a universal service fund to provide continued support for this national treasure, then that is what we must do. All providers of telecommunications should contribute to the fund including long distance carriers, bypassers and private systems.

It is imperative for the interest groups that are benefiting so enormously from deregulation, competition and the break-up of AT&T, to shoulder some of the burden that these actions are shifting to the residential ratepayers. The Bill McGowans' and the Charlie Browns' of this world would do well to adopt the attitude of Boston businessman Edward Filene who once remarked about taxes, "Why shouldn't the American People take half my money from me? I took all of it from them."

What we are asking here today is that these enterprises give up just a very small part of their not inconsiderable revenues to ensure that the American people have the ability to afford basic telephone service—to communicate with their neighbors, their relatives and their government.

As you are probably aware, state commissioners and BOC representatives have met several times in the last six weeks to discuss our mutual interests in federal telecommunications legislation. While we certainly have our differences on some of the issues that might be addressed in legislation, we have come to at least informal agreement on several broad principles. These include: (1) establishment of the universal service fund, with a broad network of contributors, and (2) an effective program to maintain universal service at current levels throughout the country.

I know that there will be strong support from the state commissions on these issues, and many others which have already been addressed in the bills filed. I am also optimistic that the local telephone companies will join the states in their push for universal service legislation at this time.

None of us wants to turn the clock back on our great advances in technology, but neither do we want to return to a time when only a few people had a phone in their homes.

It is well to remember one of the great miscalculations in recent political history which occurred in 1936. In that year, the Literary Digest, then the most popular magazine in the country, conducted a postcard poll on the upcoming presidential election. The results of the poll predicted a landslide for Alf Landon, who, in reality managed to carry only two of the forty-eight states.

Where did the Literary Digest go wrong? It seems that in addition to polling its own subscribers who were better off than the average voter, the magazine used the names and addresses of two other "affluent" groups—automobile owners and, you guessed it, telephone subscribers. In the 1930s, the vast majority of the country's population couldn't afford a telephone, but they sure could cast a vote. If Congress reaffirms our national policy commitment to universal service this Session we can all rest more comfortably that this situation will not recur any time soon.

ANALYSIS OF PROPOSED/PREFERRED UNIVERSAL TELEPHONE SERVICE LEGISLATION

Issue	Packwood proposal	Wirth proposal	Preferred position
Access charges	Overturns (prohibits) FCC customer charge ($2-$4/mo). Gives all access setting authority to the FCC. Includes bypass/private systems	Repeals current FCC decision FCC sets rules and regs Tariff authority for direct access delegated to States. Delegation conditioned upon adherence to statute and FCC rules and regs. Access charge designed to assure universal service at affordable rates. Includes bypass/private systems FCC allocates joint plant FCC may overturn State tariff decision on appeal. Provides a transitional buffer until the access structure is firmly in place.	Preliminary support for Wirth approach with modifiers to provide for a limited FCC role and more meaningful State input in access setting process.
Universal Service Fund.	Includes toll carriers, bypass/private systems. Telcos receive 90 percent of Universal Service costs above 110 percent of the national average (100 percent above 250 percent NL). Provides for $100,000 fine for unlawful avoidence of Universal Service payments.	Includes toll carriers, bypass/private systems. Telcos receive a percentage (determined by the Universal Service Joint Board) of costs in excess of 115 percent of the national average. Includes a transitional account (floor) to insure overall support for local service at 1982 levels.	Support inclusion of bypass/private systems; Packwoods percents; Wirth transitional account.
Universal Service Board.	5 FCC/4 State members Administratively final decisions	3 FCC/4 State members Makes recommendations to FCC for final action. Provides for appointment of joint board staff.	Equal State/Federal representation. Administratively final decisions. Specific funding, staffing, travel provisions.

ANALYSIS OF PROPOSED/PREFERRED UNIVERSAL TELEPHONE SERVICE LEGISLATION—Continued

Issue	Packwood proposal	Wirth proposal	Preferred position
Jurisdiction	Intrastate long distance given to FCC. FCC given jurisdiction of NTS costs—equal to 60–80 percent of local exchange plant.	Leaves intrastate long distance with States. Leaves intrastate NTS recovery with the States.	Strong preference for Wirth approach.
Lifeline service	FCC/States ensure access to basic telephone service by "natural persons".	States establish rules for lifeline service. Defined as minimum service for low-income residential customers.	Wirth approach preferred.
Primary telephone instrument.	Not addressed	State PSC's may require local Telco to offer the option for customers to lease a basic telephone set and associated wiring. Rates are fully compensatory for the Telco's offering.	Wirth approach preferred.
Depreciation setting.	Not addressed	Retains State authority to set depreciation for intrastate plant (reverses FCC preemption).	Strong preference for Wirth approach.
Inter-exchange tariffs.	No provision	Retains present nationwide averaging of toll rates for AT&T and its partners.	Some nationwide averaging makes sense for the transition to keep service available as competition grows.
Cross subsidies	No provision	No cross subsidies between regulated and unregulated utility operations. Lists Yellow Pages as a regulated service—with profits attributable to monopoly service.	Support the concent of no cross subsidy. Also should treat cellular mobile radio service profits as regulated and attributable to local monopoly service.

Chairman **Packwood**. Thank you.

Commissioner Rudd.

Take that microphone and talk right into it, so we can hear you.

Ms. **Rudd**. Thank you, Mr. Chairman.

My name is Lisa Rudd. I am the commissioner of the Department of Administration in the State of Alaska. I am appearing here today in behalf of Bill Sheffield, the Governor of the State of Alaska. With me is Juliana Guy, who is the deputy commissioner in the Department of Administration for Telecommunications, the Department of Administration in Alaska, being responsible for telecommunications policy for the State.

We appreciate the opportunity to present our views on a subject that is critically important to all Alaskans and to all Americans.

At the outset, I want to express Alaska's deep appreciation to the chairmen of the respective committees and subcommittees, Senator Packwood and Congressman Dingell. We remember particularly, Congressman Dingell, the effort that you put into the D–2 issue on behalf of the State of Alaska, and we remember it.

Chairman **Dingell**. I remember it with affection. You were a pleasure to work with and for.

Ms. **Rudd**. Well, we still appreciate the effort that you put into it. It was wonderful.

Congressman Wirth also, we are happy to recognize the effort that he is putting into this issue. We also appreciate the many Members of Congress who have supported this effort and the strong leadership that Senator Ted Stevens of Alaska has provided for Alaska and all of rural America on this issue.

Modern communications is not a convenience in rural areas such as Alaska. Communications are essential to life itself and to the continued development of my State and rural areas of all the other States in the Nation. Rural areas simply cannot develop and will not develop where adequate telephone service does not exist. The Congress must appreciate the potential impact of dramatic telephone rate increases on rural telecommunications.

Alaska is not different from the rest of rural America. We are unique only to the extent that we are an extreme example of what distance, and climate, and environment, and dependence on affordable communications systems can mean to a people.

We are not here to oppose competition in communications. We accept the national policy of interstate telephone services and customer equipment provided on a competitive basis. We recognize that such competition requires changes in the way telephone companies interconnect with each other and how telephone costs are allocated.

However, the FCC's recent decisions, if not modified, will greatly exacerbate the already substantial differences between urban and rural access to telephone service. Unless Congress steps in, these decisions will result in dramatic increases in rural exchanges.

According to estimates prepared by the Rural Electrification Administration, if the FCC access charge and Joint Board decisions take effect, one Alaskan community would be faced with monthly local exchange charges of $74. That is in 1981 dollars. That does not include the cost of any long distance calls, just local service and long distance access charges. Of the 11 Alaskan telephone companies in the REA study, the lowest—the lowest basic monthly rate under the FCC decisions is estimated to be over $35.

The Lieutenant Governor of the State of Alaska, Steven McAlpine, testified before the FCC's Joint Board earlier this year, urging that body to insure that basic telephone rates for all Americans be kept within 110 percent of the national average. The States of Idaho, Montana, New Mexico, North Dakota, Oregon, Washington, and Wyoming joined Alaska in taking this position.

Since then, the entire Western Governors Conference, at the urging of Governor Sheffield, has unanimously adopted a resolution calling for basic telephone rates to be kept within 110 percent of the national average.

Finally, the State of Alaska has petitioned the FCC to reaffirm its policy that interstate long distance rates between the offshore points, including Alaska, should remain integrated with the nationwide average rate schedule. Further, I would tell you that Governor Sheffield will present the same resolution which was passed by the Western Governors last month at their conference to the National Governors Conference in Portland, Maine, next week.

Congress should not wait to act until all of the dust has settled. The cost of acting later rather than now can only go up.

For 50 years the Congress has had the policy of promoting universal service. This policy has served the Nation well. At a time when telecommunications will play an even more important role in the lives of all Americans, we can ill afford to turn away from this objective.

In summary, the State of Alaska would like to make the following points:

First, any rural areas of the Nation will suffer dramatic increases in their telephone rates if Congress does not act before January 1, 1984.

Second, rural Americans should not pay more than urban Americans for telephone service.

Third, every American is entitled to affordable telephone service.

Fourth, the principle of long-distance rate integration is sound public policy.

And, fifth, the State of Alaska supports legislation which would keep local and long-distance rates within 110 percent of the national average.

Thank you very much, Mr. Chairman. I would be very glad to answer any questions you may have.

[The statement follows:]

STATEMENT OF LISA RUDD, DEPARTMENT OF ADMINISTRATION, STATE OF ALASKA

I am Lisa Rudd, Commissioner, Department of Administration of the State of Alaska. I am appearing on behalf of Bill Sheffield, Governor of the State of Alaska. I am accompanied by Julianna Guy, Deputy Commissioner for Telecommunications.

We appreciate the opportunity to present our views on a subject that is critically important to all Alaskans and to all Americans.

At the outset, I want to express Alaska's deep gratitude to the chairmen of the respective committees and subcommittees—Senators Packwood and Goldwater and Congressmen Dingell and Wirth—for recognizing the importance of legislation to protect the availability of universal telephone service for all Americans, including those in rural and remote regions such as Alaska. We also appreciate the many Members of Congress who have supported this effort and the strong leadership Senator Ted Stevens has provided for Alaska on this issue.

Alaska is a land where injured people are forced to ride for hours and miles on sleds, boats, snowmachines and in small aircraft before they can obtain preliminary medical treatment; where a simple call to order parts for critical repairs to speed a commercial fisherman on his way may be delayed for days until he can reach a phone.

Of Alaska's nearly 300 communities, 63 have no health clinic or doctor's office. Twelve Alaskan villages are more than 800 miles from the nearest hospital. Less than one percent of Alaska is accessible by road. Although more than twice the size of Texas, Alaska has fewer roads (9,000 miles) than Rhode Island, fewer paved roads (2,800 miles) than New York City. Of Alaska's nearly 300 communities, only 35 percent connect to a road system. Sixty percent of its 365 public airports are rated inadequate.

Modern communications are not a convenience in Alaska. Communications are often essential to life itself and to the continued economic development of the State. Rural areas simply do not develop where adequate telephone service does not exist.

While we are very proud of our "Great Land", we in the State government are acutely aware of the necessity for and our responsibility to foster the development of a viable, affordable communication system over a vast area.

Due to the lack of adequate road infrastructure and severe weather conditions, we must rely on telecommunications to an extraordinary extent. We must carefully coordinate the delivery of supplies and resources and use telecommunications more extensively than travel to communicate with one another. Even our elementary and secondary schools are increasingly using teleconferencing.

We recognize the role which communications has played in the development of the human and natural resources of rural America. Universal telephone service, together with rural electrification and our national highway system, has greatly improved the quality of life in rural America and has enabled our entire Nation to benefit from the human and natural resources thus developed.

The Congress must appreciate the potential impact of dramatic telephone rate increases on rural telecommunications. Alaska is not different from the rest of rural

America. Alaska is unique only to the extent it is an extreme example in terms of distances, climate, environment, and dependence on an affordable communications system.

We are not here to contend that the Congress should not allow for a competitive communication environment to prevail. We accept the national policy of interstate telephone services and customer equipment provided on a competitive basis. We recognize that such competition requires changes in the way telephone companies interconnect with each other and how telephone costs are allocated.

Working together, we can develop balanced and fair telephone policies. We can develop fair competition that does not wreak havoc on communications systems in high cost areas. We can minimize differences in the price of telephone service between urban and rural subscribers.

The FCC's recent decisions, if not modified, will greatly exacerbate the already substantial differences between urban and rural access to telephone service. Unless Congress steps in, these decisions will result in dramatic exchange rate increases in many rural exchanges.

In fact, last week a rural telephone company in Washington state asked the Washington PUC for a 212 percent rate increase in direct response to its anticipated increases in costs as of January 1, 1984.

According to estimates prepared by the Rural Electrification Administration, if the FCC access charge and Joint Board decisions take effect, one Alaska Community would be faced with monthly local exchange charges of $74 (in 1981 dollars). That does not include the cost of any long distance calls—just local service and long distance access charges. Of the 11 Alaskan telephone companies in the Rural Electrification Administration study, the lowest basic monthly rate under the FCC decisions is estimated to be over $35.

But Alaska is not unique. The Western Rural Telephone Association is concerned that local rates for their members will increase to between $25 and $40 a month and that 20 percent to 40 percent of rural customers will no longer subscribe. Here, we're talking of Idaho, Montana, California, Arizona and other western states—not just Alaska.

Many, if not most of the residents of Alaskan Bush communities live at or below the subsistence level. As desperately as they need reliable communications, they are less able to pay for telephone service than their city brethren. Without some sort of substantial support, these high cost, remote communities simply cannot be served.

The Alaska Public Utilities Commission and the Alaskan exchange carriers have been struggling mightily to get telephone service into more Bush communities. With the present level of interstate support, we are attempting to introduce telephone exchange service for the first time ever into about 70 new communities within the next three years. If this level of support is substantially reduced, not only will these projected gains be lost, but we may even lose existing service in some communities.

Approximately one-third of all Alaskan communities have no telephone exchange service at all today and Alaska already has the most expensive telephone service in the nation.

The average Alaskan Bush telephone in 1978 required supporting revenue of $2,600 per year for local and toll services. This compares with a Bell System average of $560. Although the average Bush user pays about $1,000 per year in charges for local and long distance service, this only covers 38 percent of the cost. Very few Bush residents could or would pay $2,600 a year for phone service.

Today Alaskans pay 20 percent more for interstate service than those in the Lower 48. And, Alaskans pay 80 percent more for intrastate long distance than interstate long distance—the highest disparity in the nation. For Bush residents almost all calls are long distance—to order groceries, to make a plane reservation, to call the dentist.

Nationwide, the investment in local exchange equipment requires annual supporting revenues of some $44 billion. On the average, about 25 percent of this cost today is paid for by interstate long distance callers. If all of this support were lost, the average Alaskan telephone subscriber in our Bush areas would have to pay over $200 a month for local and long distance service.

The decisions of the FCC and its Joint Board are also inadequate to protect against the dangers of substantial increases in long distance service in rural areas. AT&T Chairman Charles Brown is unsure whether his company is in a position any longer to maintain nationwide averaged long distance telephone rates. We are concerned that these rates will substantially increase in high cost areas, to the detriment of the State and the Nation, unless Congress acts.

The Lt. Governor of the State of Alaska, Stephen McAlpine, testified before the FCC's Joint Board earlier this year, urging that body to ensure that basic telephone rates for all Americans be kept within 110 percent of the national average. The States of Idaho, Montana, New Mexico, North Dakota, Oregon, Washington, and Wyoming joined Alaska in taking this position. In addition, the Western Governors' Conference, at the urging of Governor Sheffield, has unanimously adopted a resolution calling for basic telephone rates to be kept within 110 percent of the national average. Finally, the State of Alaska has petitioned the FCC to reaffirm its policy that interstate long distance rates between the offshore points, including Alaska, should remain integrated with the nationwide average rate schedule.

We are not asking that only Alaskans or only rural Americans be protected. We recognize the importance of communications to every person. We believe that all Americans, regardless of where they live or the level of their income, should be entitled to basic telephone service at reasonable rates.

There are those who would argue that Congress should wait to act until all the dust has settled, until we have all of the facts. If Congress waits until we know precisely what the impact is, it will be too late. The costs of acting later rather than now can only go up. Many Americans, rural and urban alike, will be forced off the system because they can no longer afford telephone service.

It is clear that unless Congress acts, local telephone rates will rise dramatically. The $9 billion in local rate increases requested to date in 1983 are not imaginary. And they are just the tip of the iceberg. We should know as much as we can, but a lack of perfect knowledge should not be used as an excuse to impose upon Americans dramatically higher telephone rates.

While the benefit of keeping rates in high cost areas reasonable and affordable can be significant, the burden on those in low cost areas or who are are volume distance users is small. There are about 250,000 telephones in Alaska. In the entire nation, there are over 180 million. In order to reduce the yearly cost of providing a telephone in Alaska by $100, it would cost the nation less than 15¢ per telephone per year. More importantly, the burden would not fall primarily on residential users if a surcharge is assessed on long distance service. It would fall on the large volume users—typically large businesses—who benefit the most from the availability of a nationwide communications network and who stand to reap the greatest benefit from the increasingly competitive long distance market.

For fifty years, the Nation has had the policy of promoting universal service. That policy has ensured that the benefits of technology are shared by all Americans, not just those living in certain areas, through averaging of long distance rates and requiring long distance users to contribute fairly to the cost of local exchanges.

This policy has served the Nation well. At a time when telecommunications will play an even more important role in the lives of all Americans, we can ill afford to turn away from this objective.

In summary:

Many rural areas of the Nation will suffer dramatic increases in their telephone rates if Congress does not act before January 1, 1984.

Rural Americans should not pay more than urban Americans for telephone service.

Every American is entitled to affordable telephone service.

The principal of long distance rate integration is sound public policy.

The State of Alaska supports legislation which would keep local and long distance rates within 110 percent of the national average.

Thank you for your consideration. I would be pleased to answer any questions.

Chairman PACKWOOD. I think we may have questions of the whole panel now, although I have only one principal question. I will direct it to Commissioner Hipp. If we decide as a matter of national policy that we do not want the access charges, that we want to continue using the long-distance rates as a subsidy for the rural and residential rates, how do we guarantee we achieve that if we do not preempt the State PUC's so that they, on a random basis, cannot institute access charges?

Mr. HIPP. Mr. Chairman, if we were to maintain the present separations and settlements, modified to meet existing conditions, we would not have any problem. We have existed with the FCC on the separations and settlements for 20 or 25 years, in joint meetings with them in arriving at the separations and settlements formula and in carrying out the interstate-intrastate separations and settlements in a way that there has never been any problem.

Chairman PACKWOOD. There is nothing under the present law, is there, under your separations and settlements policy that prohibits the State PUC's from going to access charges if they want to intrastate?

Mr. HIPP. There is nothing that prohibits it to my knowledge, and I guess in a way Judge Greene's order may require it, and that might be the additional factor that we would have this year that we have not had in previous years. If Congress requires the FCC to change its presently proposed access charge, I am confident that no State PUC will retain it for intrastate toll, because they would not remain in office long if they did. We would have to have something that would fit a label called an access charge, but it could be calculated in the same way as separations and settlements have been calculated in the past.

Chairman PACKWOOD. I have no overwhelming desire for preemption as a matter of policy. I am just trying to find a way to make sure that we do not have some of the State PUC's attempting to do what we might be trying to stop the FCC from doing.

Mr. HIPP. Well, I think that the PUC's have a responsibility to have an access charge that will meet the needs of their State, and it has got to be compatible with the national access charge.

I think there may be some individual geographical or other areas in a certain State, or economic areas, that would require the PUC to have some modifications in their access charges. North Carolina has one or two small modifications in the existing separations and settlements formula, but they have not materially affected the availability of telephone service in North Carolina or the effect on the interstate telephone service that comes in and out of North Carolina.

Chairman PACKWOOD. Do any of the other three of you want to comment on that question?

Ms. LEISNER. I believe your question was, if you gave the ability to the States to set access charges, what would stop us from doing what the FCC has done, is that correct? I think the difference is that we are much closer to the people in the States and we are more committed to universal service.

I think if we had done what the FCC did last December 22 none of us would be here today. I mean, we would have just been thrown out.

Chairman DINGELL. As a matter of fact, none of you would be holding public office today.

Ms. LEISNER. That is right.

Chairman DINGELL. I think that is a better way of putting it. That is something the FCC ought to keep in mind.

Ms. LEISNER. Exactly. We have a much greater concern with local rates and keeping everyone on the network.

Chairman PACKWOOD. Let me ask you this. In essence, the answer to my question is pragmatically what is going to keep you from doing it.

Mr. SCHNEIDEWIND. There is a big difference between a total across-the-board preemption of interstate rate regulation on the one hand and a mechanism which makes it so profitable to mimic the newly established Federal mechanism that one would be insane not to do so. In a sense, we have the reverse of that now. The FCC's access charge decision clubs you at the State level, and why not woo us at the Federal level to mimic the new system, as it could be designed to do.

The other thing is that, even if that were not technically feasible, which I think it is, it would be a lot more palatable medicine for you to narrowly speak as to what the national system is and that we might not want or be able to do certain things, than to take over the whole authority.

Chairman **Packwood**. That is a fair statement, because I think what I at least intended in drafting my bill was to make sure that the residential and rural customer is not going to be hit by a State PUC with the equivalent of the same charge we are trying to stop the FCC from imposing. As a matter of philosophy, I have no desire for preemption for the fun of it.

Mr. **Schneidewind**. You can make it so worth our while to mimic the Federal mechanism, as the FCC has made it horrible not to, to imitate theirs, that I think you can win our hearts and minds pretty easily.

Chairman **Packwood**. The Federal Government is not notoriously good at that.

Congressman Markey.

Representative **Markey**. Thank you. Thank you, Mr. Chairman.

Ms. Leisner, Florida is a high-cost State, is it not?

Ms. **Leisner**. That is correct.

Representative **Markey**. But is it not a high-cost State largely because it is a high-growth State?

Ms. **Leisner**. That is correct.

Representative **Markey**. You have got areas like Tampa and other areas that have all new equipment in.

Ms. **Leisner**. We have two reasons why we are a high-cost State: First, we are a high-growth State and high-growth States are in general high-cost States.

We also do have some rural areas, like in the panhandle, which would be high-cost regardless of the growth of the rest of the State.

Representative **Markey**. I understand that, and I have a great concern for the poor and those in the rural areas that cannot afford their service.

But I do have a problem with Bostonians subsidizing Sun Belters—that is, people moving to Tampa, moving to all of these States down there, and as a result having to make a tremendous investment in all new equipment that goes right into that rate base. I oppose formulations that require we up in Detroit or Boston or Malden to pick up the tab for Tampa and Tempe. I have very, very great reservations about that.

Ms. **Leisner**. I understand that and I heard those concerns this morning. The point is, though, that those revenue flows already occur through our separations and settlements procedure, because we have average toll rates. There are subsidies now flowing between the States, between high cost and low cost, and it has always been the philosophy to have a national policy that everyone in the country should be able to reach everyone else, and that is how that entire subsidy procedure got started.

So we are not really, in having a universal service plan, you are not creating any new kind of philosophy here.

Representative **Markey**. The inherent underlying philosophy of universal service remains intact. No one disputes that. Yet the question before the Congress and before the FCC is who should bear the cost in proportion to other parts of the user base? And for us who have lower cost bases and investment in past eras in hooking into the loop, we have to ask ourselves how much we want to subsidize people who are moving to Dallas, who are moving to Tampa or Phoenix or wherever. How much of that cost should be borne by those who want to create this new base? What are we going to do to help those that are in need, the poor, the elderly, the rural?

How does so-called universal service subsidy, subsidies for high-cost areas, help poor or elderly consumers, say in Detroit or Boston? We need something more, do you not think, Mr. Schneidewind?

Mr. **Schneidewind**. We need something, pardon?

Representative **Markey**. We need something more than just a high cost subsidy. We need some kind of lifeline service subsidy, do we not?

Mr. **Schneidewind**. You know, you are looking at an iceberg and there is a little portion that is above the water, which is the universal service funds we have been talking about, which prevent great variations in the cost of service throughout the Nation. That is small compared to the amount of money that has been in the system to prevent everybody's rates from going up two or three times. So let us recognize there are two problems here: The first problem is that we have to try to prevent everybody's rates from doubling or tripling, and obviously that is a matter of great concern to us.

We have in place a mechanism, and every bill I have seen that addresses this question has its own mechanism, that creates not a solution but a process, a process that brings together, as the legislative process does, representatives from these different communities and has them strike a balance, a balance between subsidy and a balance to the fact that if a well-to-do person in Detroit can call their poor aunt in rural Oregon that is a benefit to them. Or if businesses can contact people in these areas, that may make service more valuable to them.

But the point is, it does not take but a fraction of the money to knock down these regional differences than it does to prevent everything from going up double or triple.

Representative **Markey**. Well, do you not think the targeted subsidies for the poor, for the elderly, makes the most sense in terms of addressing the problem?

Mr. **Schneidewind**. Let me talk about that, because I think there are grave problems with that. Let us go over them.

No. 1, the mechanisms to do that, whether you take a traditional sort of public assistance approach or technical metered, measured, or other options, those mechanisms, Representative, are not in place today. And to get them in place will be very expensive and time-consuming. I think we all recognize that.

These increases are going to hit now. They are hitting now. We cannot wait. So we need some help now.

The second thing is that if you put into place a mechanism of low-cost options, we have many counties in Michigan in which the unemployment rate in the Northern Peninsula is over 40 percent. What if every one of those people migrates to a low-cost subsidized system? The fact of the matter is, the revenue shortfall will be so great for that telephone company that it will be visited upon the remaining people and yet more of them will drop off.

Representative MARKEY. My time has expired.

I do not think anything that we are debating today, not access charges or depreciation or anything else, is as important as getting targeted help to the elderly, poor, to the people who are perhaps going to be forced off the network. And that is why my bill places such an emphasis on targeting that help to the people who need to have that kind of assistance.

Otherwise I am scared that we will have built a system in which we are giving subsidies, but subsidies only to the people who do not need them. As a result, we would siphon off the revenues that should be given to the people who are really going to need it, who cannot move to other parts of the country, and who are in fact going to be pushed off the system. And that is my real problem.

Thank you, Mr. Chairman, very much.

Chairman PACKWOOD. Chairman Dingell.

Chairman DINGELL. Thank you, Mr. Chairman.

Ladies and gentlemen, I would like to thank you all for being here. We are delighted to see you back here.

I do remember the D-2 fight and I remember my visit to Alaska, and I look back on that with pleasure and respect. My regret is we did not do better.

We have many questions to ask. First, Mr. Hipp, you are here representing NARUC and have presented a statement on their behalf. Can you give us an analysis or statement of what the rate increases will be if the two bills now being considered are not enacted into law, keeping in mind the FCC access charge decision and the bypass situation?

Mr. HIPP. Mr. Chairman, we will do that.[1] We would certainly be able to get an estimate from each State. I think that they are being made and we will certainly provide that.

Chairman DINGELL. The question has been raised about the pending rate increases in the several States. There is an increased number of applications from the local operating companies which are very, very large. Are any of those related to the question of bypass or access charges?

And are those rate increases something which are to inherent in the economics of telecommunications services in the States or other parts of the AT&T breakup now pending before Judge Greene?

Mr. HIPP. There have been increases that would be attributable to nearly all of those things that have been mentioned. The AT&T divestiture has cost revenue to the local exchanges, that is having to be made up in local rate increases.

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[1] The information was not received at the time of going to press. If received at a later date it will be retained in the committee files.

The loss of the toll that has been mentioned, intrastate toll, the loss of customer premise equipment, are the two main ones, and I think the loss of an economy of scale in purchasing at low price some of the equipment that they will have problems in buying on the same basis now.

Then, on the other hand, the FCC orders, even aside from access charge, have increased the depreciation rates, and the customer premise equipment orders, have cost money to the local exchanges from the loss of customer premise business.

Chairman **DINGELL**. The Perl study was mentioned. At your convenience, would you please submit a critique of that study for purposes of the record? Each of you may do it independently or you may do it jointly, or you may have it done by the NARUC staff.

Ms. **LEISNER**. Could I comment just for one moment on the Perle study? Because I have heard what happened earlier today.

Let me just explain, there are two Perl studies. The first one was submitted in the AT&T divestiture suit in support of keeping AT&T together. It was sponsored by AT&T and it showed the percentages of people that would drop off the network if a certain percentage of the phone bill increased.

For example, the copy of it here, using the base that approximately 92 percent of our people were on telephone networks at the time of the study, if rates increased 200 percent, which is exactly what the Texas increase is, the percentage of people on the network would drop 20 percent. It would go down to approximately 72 percent.

Chairman **PACKWOOD**. Did you say this was a study done for AT&T, which they presented in the record in defense against the breakup?

Ms. **LEISNER**. In support of AT&T, in defense of the breakup.

Now, the second Perl study that they mentioned, the revision, did not revise those percentages. It did not change the elasticity of demand in the study. All it did was narrow it down to the $2 access charge. So the dollar amount changed, and they made it a much smaller scope of study.

They said, well, if it is only $2 very few people would drop off. But it is the same study, the same elasticity of demand. They just focused it differently in the second revised study.

Chairman **DINGELL**. So what you are saying is you would get a smaller initial dropoff on a $2 rate increase as opposed to an immediate 200-percent rate increase. But it must be assumed, given the elasticity of demand for telephone service, that about the same number of people would drop off eventually, is that not correct?

Ms. **LEISNER**. Exactly.

Mr. **SCHNEIDEWIND**. There are two other points. The second Perl study focused only on the $2 charge, if you want to call it that, ignoring the depreciation increases, the loss of toll revenue, which in the aggregate are giving us a 100-percent increase and according to the Perl data would lead to a dropoff of 10 percent.

The most recent review I have seen of all of this literature comes, oddly enough, from the FCC itself, and I am surprised they did not mention it this morning. In appendix G of their December 22 access charge decision, 78-72, they said that "most of the measures of price elasticity fall around negative 0.1."

That is, a 10-percent increase in price will lead to only a 1-percent decrease in the quantity purchased. Now, this is the FCC evaluation, which means that they are saying in general terms the literature that they have seen and reviewed indicates that the 100 percent price increase we are expecting will lead to a 10-percent dropoff.

Chairman DINGELL. You used a higher figure in terms of elasticity, did you not?

Mr. SCHNEIDEWIND. No.

Chairman DINGELL. We heard 14 percent.

Mr. SCHNEIDEWIND. I said that is a low end and that in Michigan we have had experiences where there is a much higher dropoff from rate increases than the Perl data would indicate. In the Michigan community that had a 60-percent increase imposed, all of a sudden 14 percent of the people dropped off.

Chairman DINGELL. Now, you indicated, however, that this is exacerbated by some additional rate changes which stimulate further dropoffs. But because you have fixed charges, which have to be spread over a smaller number of ratepayers, the law requires an upward adjustment of rates. This will trigger further dropoffs; and this phenomenon will probably occur in at least three identifiable instances.

Was that not your comment?

Mr. SCHNEIDEWIND. That is exactly right, Representative. And that is what I call the Penn Central syndrome, because that is the very phenomenon that almost destroyed our railroad system in the sixties, which was losing traffic, responding to the loss of traffic by raising prices to the remaining traffic, which caused more of it to drop off, until the point where there was so little traffic that the system literally collapsed.

That is the syndrome that we are getting into with this level of rate increase.

Chairman DINGELL. I would appreciate further comments submitted for the record, if you please. Our time is so constrained here.

Let me just observe, we have a splendid editorial which was written in the Detroit News in my boyhood. It described the continued process of cost increase, of charges to riders of the DSR together with continued cutbacks in services. Finally, it indicated that the citizens of Detroit rose in outrage and burned the last remaining DSR bus and terminated the whole problem.

I suspect it is not beyond the realm of possibility that, while they may not be burning telephones, they may be burning business representatives of the telephone companies or Members of Congress who do not do something about this matter.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Congressman Wyden.

Representative WYDEN. Thank you, Chairman Packwood.

I do appreciate all of you being with us. In effect, we are all on the front lines. When rate shock sets in, the people they come to see are you and us. I would just like to explore a couple of areas that I think are contributing to that rate shock.

One area that we are going to be debating is depreciation. I think everybody in this room understands that we want the communications industry to be able to take advantage of developments in technology. All of you have made it very clear that you think that the States ought to have the authority to prescribe the classifications and the methods.

And what I would like to ask of each one of you is, what difference do you think that would have for the ratepayer? What difference would this mean for the ratepayer if you had the authority over depreciation considerations?

Mr. **Schneidewind**. Could I give an example? And it is one that stems from a recent Michigan Bell rate case that was settled in June. This case was filed and there was a request to go very quickly under methodologies supported by the—well, by Bell and the FCC staff—to the remaining life concept to take care of reserves that had not been funded in the amount of over $400 million.

The methodology which was urged by the FCC staff to get to remaining life would have and will increase rates in Michigan by $2.55 if they overturn or they succeed in seizing control of this area, whereas when we tackled remaining life we adopted the concept, but we took care of this huge reserve problem and amortized it over a 10-year period. Now, in dollars and cents what does that mean? It is a $1.25 impact instead of $2.55.

So yes, you know, we did not get there as fast as the FCC or Michigan Bell would have liked. On the other hand, we made a commitment to get there, we set up a funding mechanism, and it is a gradual transition, and that means $1.25 per customer per month in Michigan. That is a 12-percent rate increase that we avoided. It gave the company assurances they are going to get their money.

Representative **Wyden**. Thank you.

Some more experiences or other comments?

Ms. **Leisner**. We had similar experiences in Florida. Just to give you an indication of how many dollars are involved here, in the last Southern Bell rate case, which was a rate case of $350 million, $135 million of that was depreciation. And the Commission finally came to a decision and, out of the $135 million requested, gave them $35 million, still recognizing the increased more rapid depreciation that is expected under the new technology, without going the full way that the FCC has done.

But it is a huge amount of dollars that are involved in depreciation, and I think we certainly should have the control because it does affect local rates substantially.

Representative **Wyden**. I appreciate that, and we would like to know of similar instances like that, because both of the bills do give the State public utility commissions this authority. We feel it is one tool that needed to deal with these pending requests for local rate hikes. And we would like to hear similar examples of what you both have told me.

In the brief time remaining, I would like to explore the question of measured service. I do not know if you were here. I was director of the Gray Panthers for about 7 years before I went to the Congress, and I have never seen senior citizens as frightened as they are now. Literally, they tell you they fear they are going to be locked out of society, that the telephone is their only link to society. That is how they solve their problems. If we change to a system of local measured service they are just very, very concerned.

I know measured service proposals are being filed. I am also greatly concerned about how this would affect small businesses. I would be interested in your reactions. Let us start with the impact of measured service on the elderly. In your opinion, can it be made to work for the low-income elderly?

Ms. LEISNER. Let me start, because we had a really interesting experience with that in Florida 2 years ago in a Southern Bell rate case where they filed for an optional local measured service offering. We had 600,000 petitions sent to us at the Commission, primarily from the elderly in southern Florida and southeastern Florida opposing local measured service. We had hundreds come out to hearings in southern Florida primarily opposed to local measured service. They were very much afraid of it.

They talked about the lifeline type services they had where they call someone every day, and how they could not afford to do that if they had to pay for every call. They talked about the phone being a lifeline to the outside world. We also had handicapped people who depend totally on the phone for their communications, who were very much frightened by local measured service.

In fact, when we had the formal hearings, people came up in busloads to Tallahassee to picket us about local measured service, and at that time we did not allow it. We have opened a separate docket looking at local measured service, but our inclination now is, the only type of local measured service we would allow would be a type of service where it would be 60 percent of your basic monthly rate and then a per call charge of something like 10 or 15 cents per call, because that is the kind of service—that is about the only kind of local measured service people will want, and the elderly do want and would like that type of service.

Representative WYDEN. My time has expired. I would only say that most of us do not want to be nay sayers. We are particularly interested in alternatives, and particularly the question of an alternative to measured service for the low income and elderly. We would like your thoughts on it.

Thank you, Mr. Chairman.

Chairman PACKWOOD. Before going to Congressman Swift, let me announce to the crowd here that we have changed the meeting room tomorrow. It will be in the caucus room in the Cannon Building. Room 345 is a larger room than we had originally scheduled.

Congressman Swift.

Representative SWIFT. Thank you, Mr. Chairman.

Last week, AT&T announced that all of the Bell operating companies' services for the disabled will be transferred to American Bell, and I know AT&T would not dream of doing anything to stymie Congress, but that will very possibly frustrate the Telecommunications for the Disabled Act. I am wondering, and I understand, Ms. Leisner, that you have some special knowledge on this, with that action, what is going to happen, in your judgment, to the specialized equipment and installation services for the handicapped after divestiture?

Ms. LEISNER. We have a real concern about that, because there are several classes of handicapped people who need specialized treatment—first of all, they need special equipment, and second of all, they also depend upon the phone for their lifeline to the outside world, more than most ordinary citizens.

Third, competition and deregulation really does not benefit them, because they are never going to be able to walk into a Radio Shack and buy the equipment that they need, so we are extremely concerned in Florida, for example. For instance, TTY's for the deaf, where you type into a key pad and have an LED readout. They are now being leased to them by Southern Bell at $21.50 a month, which is at cost. We are concerned that they still be able to get that type of equipment, as well as equipment for other handicapped people, and that they will be able to afford it.

Now we are talking about $30 a month rates, which would be in addition to what they would have to pay for that leased specialized equipment. So I think there is a great concern that the handicapped, who depend so heavily on the phone, may be hurt more than the ordinary citizen in this divestiture.

Representative SWIFT. A number of groups representing the disabled, I understand, have expressed reservations about this proposal to transfer the operations to the parent company. I understand that AT&T has agreed to meet with these groups and, Mr. Chairman, I would like to ask unanimous consent to insert in the record several letters from the Paralyzed American Veterans, the National Association for the Deaf, and the American Council for the Blind.

Chairman PACKWOOD. Without objection.

Representative SWIFT. Thank you very much, Mr. Chairman.

Eric, good to see you again.

Mr. SCHNEIDEWIND. Good to see you, Congressman.

Representative SWIFT. I would just like to explore the carrot and stick approach you were discussing with Chairman Packwood earlier. Namely, as goes the way the Federal Government establishes its mechanism for making—for setting rates, does not the State more or less have to follow along, whether it wants to or not, simply because in addition to whatever inducements or threats may be implied, it just keeps a consistent process, does it not?

Mr. SCHNEIDEWIND. I think that whole issue of how to handle the separations process or a successor to it if the access charge is not used, you can first of all obviously design it to be very attractive. I am very concerned, and I want to state this concern here and now, that this issue of regionalism or State interest or regional interest be dealt with in a statesmanlike fashion, certainly one that is fair to people.

We do that now. We argue out the questions. We have people from different regions and different interests just as Congress does, and come up with solutions we can all live with. But there are some new ideas and, I think, some fairly exciting new ideas on the horizon of people talking about whether or not it would not make sense to focus the equivalent of the universal service fund on exchanges rather than State by State, or maybe company by company.

This might mean that there is a better targeting of money to where it is needed rather than, you know, getting down to a fine point.

Representative SWIFT. I think you also made the point earlier, which I think is essential, if you truly understand the concept of universal service, and that is that the person in a large Northern city that wants to reach perhaps their mother or an aunt in a small rural community benefits from affordable rates in the small rural community.

It is not simply some kind of interregional subsidy. It is rather a means of maintaining a national telephone service.

I also saw some figures that would indicate that about the maximum that might flow would be something like a penny a minute on a long distance call. Now, if you have managed by Federal legislation to save that person in the large city $8 a month on a national average—I figured it out—you are going to have to talk on long distance 13 hours, plus, in order to use up the $8 they say before they ever start sending a penny anywhere else, and I think if we start regionalizing this, and start getting into some formula like that, we are all going to sit here and bicker to the point that we are going to lose it all. We are going to lose universal service. We are going to get the $8, and we are not going to come up with a solution.

And I agree with you, it is terribly dangerous to start this kind of regionalism debate, which I think is being fostered, in order to instill dissension, as a matter of fact, in the deliberations.

Thank you, Mr. Chairman.

Mr. SCHNEIDEWIND. One thing, if I could add another antidote to that problem, and it is one I would like to suggest for your consideration, is granting to the States the authority necessary within their State boundaries if they feel a need to tackle even some regional or some exchange differences, or to hold down rates, to be giving them the authority to tailor charges to all telecommunications users to adjust the rates for everybody, so that the whole State does not go up twice or three times, to create in effect two pools, a national pool and a State pool, with authority at the State level if it wants to move further than Congress to move further.

This might get us out of the trap of being forced into handling it all at one level. It is a thought, just a thought.

Representative SWIFT. Thank you.

Chairman PACKWOOD. Senator Lautenberg.

Senator LAUTENBERG. Thank you, Mr. Chairman.

I was interested, Mr. Schneidewind, in your comment about where service is needed. You talk about the high cost areas. Is that your extended definition of where it is needed?

Mr. SCHNEIDEWIND. I think we have several problems. We have tackled in the past successfully compromises which prevent extreme variations between the cost of service because of the cost of the plant involved, and in the future, I am confident that a process of bringing different interests together and having a compromise will continue to provide a solution that is economical. It is not a huge amount of money.

The other place where it is needed clearly, and I know your interests are to insure that people of all income levels do have a telephone or telecommunications mechanism in their homes that they can use, and we do need to be thinking about that. We do need to be looking at whether there is a more efficient way to do this than we had in the past, and I do not close the door on that.

But let us remember—you know, I have been involved with trying to set up heating assistance programs for low-income people for the last 7 years of my career at the PSC in Michigan. I have not been very successful, I am sorry to say. We have got zero interest insulation programs, free insulation, this sort of thing, but we have not solved that problem, because I know the administrative difficulties are hideous of reaching out to people and providing them a special rate for some electric or gas or telephone service.

So what I would urge you to think about is that while there should be some sense that we must proceed to look for a more efficient way of handling the needs of the poor and the elderly, and maybe do it less expensively than it is now, I would love it if we could, but that will not happen quickly, and it probably will not be simple, and meanwhile, let us not let the system be destroyed.

Senator LAUTENBERG. I guess what we are trying to do is to remake by legislation the AT&T system as it existed before, because we are trying to get the parts of the system that were subsidizing local residential service to pay a share of that subsidy again. If you were here this morning, you heard me kind of reminisce a little bit and wish that the system were back together again. I think many people share that view.

But the system has been changed, and my concern is not about those, regardless of income level, who want subsidized telephone service. I am not as concerned about the $200,000 a year income family, or the $150,000 or $100,000 a year income family as I am about those who just cannot afford to come up with the $2 or $3 a month more. And I think that is where we have to focus our attention.

I also think we have to be concerned with the flow of money between the regions, despite the fact that we do not like to regionalize. Some of the proposed bills are asking one region to pay for another region's inefficiencies or geographical difficulties in supplying service, and it is a devil of a problem. We are going to have to struggle to come up with something that is equitable for all parties.

Ms. Rudd, I would like, if I may, to address a comment to you. In your testimony, you state it should be a national policy that rural people should pay no more for telephone service than urban people. I do not know if the difference between rural and urban rates is as you assume. New Jersey, for your information, is the most densely populated State in the Union. We are the ninth largest State in the Union in population, but we have rural areas, too, in the southern and western parts of my State. The people in those areas pay less than people in some cities elsewhere.

Nonetheless, what you are proposing would have a far-reaching impact if adopted as a general principle. Are you not saying that when it comes to what we decide are the basic necessities of modern life, all Americans should pretty much pay the same? I am not sure that I agree with that principle, but I would like to explore it just a minute.

In north New Jersey and metropolitan New York City, the cost of electricity, and you know this is coming, is not 110 percent or 115 percent of the national average. It is more like 150 percent of the national average. You, Ms. Leisner, have a very distinct advantage. You do not have to buy as much fuel down there to heat homes. The cost of electricity in New Jersey is 300 percent of what it costs in the Pacific Northwest. Would you suggest that those cost disparities be evened out?

Ms. RUDD. Are you talking about fuel costs?

Senator LAUTENBERG. Yes.

Ms. RUDD. Senator Lautenberg, that is another subject which is of great interest to Alaskans, because I challenge you to pay higher fuel costs than the people in bush Alaska. I cannot quote you figures, but I know that it is true that fuel costs in rural Alaska are of extreme concern, as they are to you.

As to telephone costs, the 'cost of communication, yes, I stated that rural people should pay no more than urban people for the use of a good, modern communications system. I think that that is a very valid national policy that should be continued by this Congress. It is a question of possibly a high-cost area being able to reach a low-cost area or a low-cost area being able to reach a high-cost area.

But in Alaska we have another element to the problem that I would like to talk with you briefly about, and that is that in large parts of Alaska and in fact about one-third of our communities in Alaska, we have no telephone exchange service whatsoever. So what we are facing is not only increased costs in the telephone system that does exist, but we are facing the possibility that the progress that has taken place during the last 7 or 8 years—I was in the State legislature when we first went into the Earth station business, so to speak, to bring telecommunications to rural Alaska. The progress that we have been going through during these last 7 or 8 years to bring modern communications to rural Alaska is going to stop dead in its tracks, and that third of our communities which have no exchange service whatsoever are never going to get it, and the ones that do have it, where they pay in the rural areas an average of $30 a month basic telephone charges—this is not long distance calls, this is just the basic monthly rate, where they pay an average of $30, we are going to look at charges maybe 2½ times that.

So, you and I share similar concerns. They have a slightly different emphasis.

Senator LAUTENBERG. I think you have a little advantage. I believe Alaska has the highest per capita income in the country. Thank you very much.

Chairman PACKWOOD. Congressman Lent.

Representative LENT. Thank you, Mr. Chairman.

I would like to ask the gentleman from Michigan, Commissioner Schneidewind, your testimony was somewhat premised on rate increases, I think you mentioned, of doubling or tripling, 200 and 300 percent. This kind of request, of course, puts mounting critical pressure on the Congress to keep that kind of an increase from taking place, but is it not true that just because a telephone company comes before a PUC and makes a demand for an increase, it is not necessarily granted, is it?

Mr. SCHNEIDEWIND. No; you know, I wish that the estimate that I gave were of the amount that was either going to be requested or even granted for all telephone cost increases. Unfortunately, it is not. It is only limited to cost increases that are almost certain to happen because of just Federal actions.

Representative **Lent**. I am told that most telephone rate proposal increases come in finally at about 20 percent of what is requested. Has that been the experience in Michigan?

Mr. **Schneidewind**. Let me give you an example. The cost breakdown of where we got the 100-percent increase, it came from three things basically, the access-charge decision, which is cast in concrete at the Federal level and forces us at the State level to a certain degree of mimicry. Otherwise, there will be a financial catastrophe. So that is one of the elements, and that has been pared back a bit this next year by the change yesterday, but it will be more next year than it would have been.

The next element of the increase, Congressman, is the depreciation preemption.

Representative **Lent**. Without getting into all of this, because my time is limited, can you tell me historically what has been the experience with respect to rate increase applications in the State of Michigan? What percentage of the increase in general has been granted in Michigan?

Mr. **Schneidewind**. Well, in the telephone area, we had a unique system for the last 3 years in which we held Michigan Bell to a cost-increase formula based on productivity increases and inflation.

Representative **Lent**. Of what percentage?

Mr. **Schneidewind**. Under our formula, we told them what they could have, and they got that every year. I do not mean to be evasive.

Representative **Lent**. No; what was that percentage?

Mr. **Schneidewind**. Because it was our formula. It was 100 percent.

Representative **Lent**. They got a 100-percent increase in their rates?

Mr. **Schneidewind**. It was a unique case. A more appropriate case is——

Representative **Lent**. Over 1 year, or a period of years?

Mr. **Schneidewind**. Let me give you the last rate case, and that is a better example. The last rate case, they asked for $450 million. We gave them $180 million. But a key factor, if we lose the appeal of the FCC depreciation preemption decision, we are going to have a great deal more money that we are going to have to give out, and that increase does not even include the loss of toll revenue from divestiture and the access charge, which are things that are going to be one for one. They are going to get probably a very high percentage of that revenue loss from us, because we know there is going to be a loss.

If the FCC says you must impose a $2 charge, it will be imposed.

Representative **Lent**. Well, if they say you must impose a $2 a month charge—we heard the Commissioner earlier today—nothing would prevent you as a regulator from softening the price shock by allowing innovative systems of price fixing for senior citizens and the poor, would it?

I mean, we know in California the elderly and the poor pay $2.50 flat charge a month. We have heard that in New York there is going to be a request for a $5 flat charge per month. The poor people in my area under that will actually have their rates reduced. I am sure that in California rates will be reduced for the poor and the elderly if that kind of a lifeline system is put in place. Can you do that in Michigan, too?

Mr. **Schneidewind**. In Michigan, we already have a low-cost budget service option for $4. And our fear is, first of all, even if we can get a waiver of access charges from the FCC, which until yesterday——

Representative **Lent**. But you heard the Comissioner say he would give it.

Mr. **Schneidewind**. There are many strings attached to that, if you look at the fine print. They make you come up with a detailed plan of where you will recover the revenue from other sources, and since nobody has seen the decision—I read the December decision, and it was very discouraging, on lifeline.

Let us say we do get a lifeline rate, Congressman, and it has no access charge, it is heavily subsidized for the poor and elderly. We have got counties with 40 percent unemployment and a lot of elderly people, and 40 percent of them are by definition poor.

If everybody shifts over to that lifeline rate, the loss of revenue to the local telephone company will be catastrophic, and will have to be loaded back on the remaining customers, many of whom will not be able to afford that.

So, a lifeline system, if it is only used by a few people, could be a very good answer. If it is used by 40 percent of the people in a region, it is a disaster. It cannot be maintained.

Representative **Lent**. I wonder if I could just have unanimous consent for a followup to Commissioner Leisner from Florida.

Chairman **Packwood**. Go right ahead.

Representative **Lent**. I understand that Southern Bell in Florida recently made a postdivestiture rate increase application for about 80 percent. Is that correct?

Ms. **Leisner**. Well, Southern Bell has not made a postdivestiture rate request. Southern Bell came in for a rate increase of $350 million this year, requesting that they use a projected test year, which would have been postdivestiture, and the Commission did not allow it, because there were so many uncertainties.

Representative **Lent**. Was any portion of that request granted, with 20 percent?

Ms. **Leisner**. They asked for $350 million. We granted them $113 million. There is one point here I would also like to make in that case. We took that $113 million, and we did not pass any of that on to local customers, because we now have the option of putting it on other places. We increased intrastate toll rates to bring them up to parity with interstate. We were below interstate. We put the rate increase on CPE. We put the rate increase in other areas. All those options will be gone next year. Next year, when we give them $113 million, it will go directly to the local residential customers.

Representative **Lent**. And you can give for the poor and the elderly a lifeline type lower payment? Is that true in Florida?

Ms. **Leisner**. Yes, but as Eric pointed out, suppose your average rates are $20, and you are trying to maintain a $5 lifeline rate. To maintain the $5 lifeline rate, you are going to have to take that revenue from your other customers, and you might have to increase the $20 rate to $25, causing more people to drop off who would want to go to the $5 rate, so it could be a disaster with high rates to try to maintain them.

Representative LENT. I thank the chairman.

Chairman PACKWOOD. Senator Riegle.

Senator RIEGLE. Mr. Schneidewind, the lifeline rate in Michigan, as I understand it, costs $4 a month. Is that correct? People get to make two calls a day. Is that correct?

Mr. SCHNEIDEWIND. I think it is probably a little less than that, but that is in the range, yes.

Senator RIEGLE. Essentially they are limited to two calls a day, and as I understand it, there are 300,000 subscribers or so who now subscribe to that limited service. Is that correct?

Mr. SCHNEIDEWIND. I think that is approximately correct.

Senator RIEGLE. That to me is a very high number. 300,000 plus people out of a population in excess of 9 million, I mean, that is a substantial number of telephone users opting for a lifeline service. Do you have the latitude in the Public Service Commission to increase that to four calls per day by administrative decision?

Mr. SCHNEIDEWIND. Yes.

Senator RIEGLE. How was the decision made to limit it to two calls? I would like a short answer, not a long answer. Why could you not just as well have said four as two?

Mr. SCHNEIDEWIND. There is a cost involved in terms of the switching gear and all of that. If you said four, and did not raise the price, you would have to be increasing the subsidy.

Senator RIEGLE. Suppose you raise the price and increase the number of calls. If you went, say, to five calls a day? Would that take the price up to $4.50 or $5, or would it jump to more than that?

Mr. SCHNEIDEWIND. I cannot say, and the problem is that that $4 rate is not compensatory. It is heavily subsidized, and what we are deeply fearful of is, let us say that everybody else's rates double. You know that there is going to be a fantastic migration onto that $5, $4 rate, and the problem is that in Michigan, for instance, there are 700,000 unemployed families.

Senator RIEGLE. I am aware of that. But let me offer you a solution. Perhaps, we should try to come up with a universal standard for a lifeline service, and let me give you an analogy.

We do this with postage stamps, and I think there is some value in a postage stamp analogy here up to a point, because we have got a national telephone system, and everybody needs to use it. We do not charge people in one State 30 cents to send a letter somewhere and somebody else 10 cents. We have found a way through a national process of a form of subsidy and cost to sort of spread this out, so there is a uniformity.

For those people who are at the low end of the economic scale, and who would otherwise be forced out of telephone service, I think that we may have to end up finding a variation of that same philosophy. In other words, what I do not want to see is a regionally targeted subsidy. There has been a lot of talk about regional subsidies here. I think you certainly would agree with me in that respect, because Michigan loses out in a regional subsidy scheme.

But if we are going to have to collect a pot of money here, and use it to subsidize a rate that keeps the low income person in the system rather than out of the system, then I think we ought to find a way to collect that money in much the same fashion that we collect it in the postage stamp area, and that is off a broad national base and where the collection mechanism is done in such a way that it does not impose a greater hardship on one area of the State versus another, one State versus another, one region of the country versus another.

I think that is the route we have to go here, but let me ask you this. In Michigan today, what does the basic service cost? Not the lifeline service, but just the standard service for a single private line with unlimited use?

Mr. Schneidewind. It is approximately $11.

Senator Riegle. About $11. What would it have been 5 years ago?

Mr. Schneidewind. Oh, I would say roughly in the $8 range, give or take a little.

Senator Riegle. Has it gone up in the last year or year and a half?

Mr. Schneidewind. It has gone up each year approximately 3 or 4 percent per year.

Senator Riegele. Is it fair to say that absent the consent decree here, that we would be seeing that kind of nominal increase?

Mr. Schneidewind. Absent the consent decree and absent the FCC's depreciation decision and absent the access charges.

Senator Riegle. So in other words there would be some slow climb in rates, but it would be within a manageable 3-, 4-, or 5-percent annual range, in your view?

Mr. Schneidewind. Yes.

Senator Riegle. When you were testifying before us in the last Congress you laid out, and I am sure you remember this, all the factors forcing an increase in rates.

I would like to know if today that information is still current. Have the components changed? Has the total changed? And I would like to have that information on an updated basis.

Mr. Schneidewind. We are trying to evaluate the impact of Judge Green's assessment of costs of network reconfiguration, and that is difficult. So is the FCC. It is a difficult thing. And then the access charge decision yesterday will have at the outset perhaps a $1 or $1.50 impact in terms of being lower than our estimate, and you have to say that, because I think that is a fair assessment, but right now I guess we will do a more detailed job. Right now I would have to say I do not expect that that assessment will change significantly, and by significant, I mean by more than 10, 15 percent.

Senator Riegle. So you are saying in the absence of any change, you estimate that rates in Michigan will essentially double within a 12-month period? That is the best professional estimate of the Michigan Public Service Commission?

Mr. Schneidewind. Yes:

Senator Riegle. Thank you, Mr. Chairman.

Chairman Packwood. I think a few people have some other questions. I know the chairman has some additional questions.

Chairman **Dingell**. Thank you, Mr. Chairman. I will try to be as brief as I can here. Gentleman and ladies, there have been a number of comments made indicating that if this bill or either of the bills pass, there may be some interregional transfers of money. On analysis of the bill, I come to a slightly different conclusion.

Am I correct in the understanding that the bill sponsored by Chairman Packwood or the one sponsored by Chairman Wirth and I would simply seek to preserve the status quo as far as allocation of financial resources amongst the different parts of the country?

Mr. **Hipp**. Well, I think the status quo would be observed, Mr. Chairman. The present system is supporting local rates through a contribution to the use of the local lines, and I think that if we continue with the high cost factor, it would do almost the same thing. I do not see that there would be any more transfer than we are having now.

It could be targeted somewhat, that is, the base that you are applying the 115 or 110 percent on, might be just the loop or it might be the entire average rate or it might be some other base that you apply the percentage to.

Chairman **Packwood**. Let me pursue this. I ask the Chairman's leave.

Chairman **Dingell**. I am delighted to yield.

Chairman **Packwood**. The opponents of this bill in some cases are attempting to convince some Members of the House and Senate that their states are suddenly going to bear a disproportionate burden in terms of money in and money out, although States do not pay this per se. It is the users that pay it. All Chairman Dingell is saying, and I am asking you to say if he is correct, that that is the present system, and we are not significantly changing the present system.

Mr. **Schneidewind**. The only difference I can tell from the present system, there is no difference inherent in the Wirth-Dingell bill and in your bill, Senator, the base of the kick-in point for contribution is 5 percent different, which would cause some difference.

As near as I can tell—and Commissioner Hipp is certainly the expert—I cannot see any difference other than that. That is it.

Chairman **Dingell**. Commissioner Leisner, do you have any comments you want to make?

Ms. **Leisner**. I think that is true. Under the separation-settlement process, that is the way it has always been. We are just seeking to maintain the status quo. We are just calling it by a different name than we had in the past. That is the only difference. And it is the same philosophy.

Chairman **Dingell**. Commissioner Rudd.

Ms. **Rudd**. Mr. Chairman, I am not an expert in regulatory matters and ratesetting, so I recally cannot respond to that question.

Chairman **Dingell**. I was troubled about this when I heard it the other day because I felt that this would cause us problems and might even cause me problems. But as I see the situation, we are preserving the status quo. The shifts of money around the country stemming from allocations of costs between long distance and local service, between the different regions, would remain, according to your comments, substantially the same as they are today.

Is that correct?

Mr. HIPP. Yes.

Senator LAUTENBERG. Would the gentleman yield, please?

Chairman DINGELL. I would be delighted to.

Senator LAUTENBERG. Could we pursue this line of questioning? We are beginning to define specific interests and concerns, I dare say.

Would you be willing to say at this point that nothing will change relative to the proportions? In other words, whatever it costs my State or any of the other low cost States would be the same in terms of the total kitty, if I can use that expression, as it has been?

Mr. HIPP. That would be my opinion.

Senator LAUTENBERG. You have studied the two committee chairmen's bills that are before us. You have not yet looked at mine, I assume.

Mr. SCHNEIDEWIND. I think the thing that maybe is leading us somewhat astray is that right now the mechanism to make this allocation, to decide the level or subsidy as between States or kick-in point for subsidy is not a fixed formula but a process that brings four State regulators and three Federal regulators in a room to work it out every now and then. What the Federal and State regulators have just worked out, thanks to heroic effort by Ed Hipp and others, is totally consistent with the approach in both bills, totally consistent with the Wirth-Dingell, and the kick-in point being only slightly different for the Packwood approach. But both those approaches would still have a body of State and Federal regulators as it is now to make further adjustments in the process which are not fixed by law.

Senator LAUTENBERG. I am not talking about the process. Before I go on, I should say that I am not familar with the appropriate protocol when one yields time. I assume the person who yields does not lose his position for the week.

Chairman PACKWOOD. I can guarantee you Chairman Dingell will take it back when he wants to.

Senator LAUTENBERG. I will be glad to turn it back.

Will you signal in some way, or do you want it back now?

Chairman DINGELL. I have other questions, but I am delighted to yield.

Senator LAUTENBERG. I will defer.

Are we going to have another round of questions?

Chairman PACKWOOD. We are going around again.

Chairman DINGELL. In light of the comments made, let me ask you to give us, as you deem appropriate, further statements for the record on the question I have just asked.

Let me ask this. As I gather, there is another question that we have had to contend with, the question of technology. As I understand it, the same technology is available to everybody. Bell has access to the best technology, local operating companies will have access to the best of technology, the competitors of Bell, MCI, and Sprint and all the rest of them, will have access to the same excellent technology.

So it has been said that the access charge plan of FCC might in some way advance technology, or that the bill that Chairman Packwood and Chairman Wirth and I have sponsored in the House and Senate might in some way impair the advancement of technology.

Is there any reason for us to be apprehensive that the FCC's plan would be better suited for encouraging new technology than the proposal that Chairman Packwood, Chairman Wirth, and I have made?

Mr. HIPP. I would not think so, Mr. Chairman. The customers that want to go into bypass will be seeking the best technology they can find under either bill. I think under the FCC plan, they will still be looking for ways to bypass, and they will be looking for any technology they can find. And under the plans in these two bills, they will still be looking for bypass and the best technology that is available, and I do not see much difference in the incentive under one plan or the other.

Ms. LEISNER. I think it is the market and competition that drives technology, not the access charge plan or any things that are in either of these two bills. It is something way beyond that that is driving the technology.

Mr. SCHNEIDEWIND. And by drafting the bills the way they have been—and I am more familiar with the Wirth-Dingell bill, but I think it is inherent in the Packwood bill—by drafting it so that the charge to maintain the system is equitable for all, for bypassers and for people on the system, what you have done is preserved a fair game, as it were, so that then technology can win out because the rules of the game are the same for everybody. So you have preserved all the incentives by being fair to all the players.

Chairman DINGELL. Now, there was a busy day—we find in reading the papers this morning that some action by the FCC with regard to both access charges and bypass took place.

I observed with some interest that the FCC did lay in place language relating to bypass.

I would appreciate your comments on that at the appropriate time and I would observe that with regard to bypass the FCC has essentially indicated that bypass charges can be laid in place, can be properly administered, and can be used to correct the imbalance that exists between those who would bypass and those who would not, depending upon the level of the access charges.

Am I correct in that assumption?

Mr. HIPP. Mr. Chairman, I have been in transit during part of this, and I am not aware of what the FCC provided for bypass charges, that is, charges on the bypassing. I am not aware of that.

Ms. LEISNER. I think we are all a little lost.

Chairman DINGELL. Would you confer on that matter and give us your best thought afterward if possible?

Would somebody else like to make a comment?

Mr. RENARD. Mr. Chairman, if I can give you my understanding of the technical matter?

Chairman DINGELL. Would you please identify yourself for the record?

Mr. RENARD. Yes. I am Bruce Renard, the associate general counsel for the Florida Commission.

My understanding is the FCC made it clear that charges could be imposed on private line service on a usage basis. Therefore, that would establish a system whereby you could measure and ascertain the benefits flowing to bypassers, private systems, and come up with a workable mechanism to assess those systems for their contribution.

Chairman **Dingell**. So does that indicate that bypass charges are a mechanism that can be used to redress any imbalance that might exist by a different level of access charges?

Mr. **Renard**. Yes, Mr. Chairman. I think that establishes the workability of that type of system.

Chairman **Dingell**. Would that be the view of the panel?

Mr. **Schneidewind**. Yes. The desirability, very definitely.

Chairman **Dingell**. Mr. Chairman, I guess I have used all the time that I am entitled to.

Thank you, ladies and gentlemen.

Chairman **Packwood**. Congressman Wyden, anything further?

Representative **Wyden**. Thank you very much, Senator.

I would like to follow up quickly on my earlier question about measured service, and I think all of you essentially share my concern about what it is going to mean for low-income senior citizens. Now I would like to talk particularly about small business and what the effect of measured service would be on small business.

In my State, Northwest Bell has filed for a measured service proposal for business. It seems to me that it is very attractive now for big business to just go off on its own, set up its own system, just bypass on the network.

I am curious about what you think that will mean for small business. Where does that leave them?

Ms. **Leisner**. Well, I can tell you when we had the local measured service proposal, the small business people did come out, especially real estate sales offices and personnel agencies, came out that were in one- or two-man offices, complaining greatly.

Representative **Wyden**. I did not quite understand that. Did you say that one- or two-person offices in your area were very unhappy?

Ms. **Leisner**. Yes, small businesses that use the phone a lot were extremely unhappy, and I think you are correct, that it is the larger businesses that can bypass, that would be encouraged to bypass if local measured service were implemented for businesses. And then, of course, the burden would fall more heavily on small business people.

Representative **Wyden**. Could you give us some of the statistics on that point? We are particularly interested in the effect on small business, and the Florida experience would be helpful.

Ms. **Leisner**. Yes.

Representative **Wyden**. Was there further comment?

Mr. **Hipp**. I do not know if this is relevant, but most of the tariffs that I have seen have had a message service that is available only to businesses all along, whether they have local measured service or not. But there are very few small businesses that I am aware of that utilize it. It is just not something they want to use. They would rather have a flat rate and pay the flat rate and have unlimited use.

I would be glad to try to furnish the figure on that.

Representative WYDEN. I think it is clear that this is something that is going to generate a great deal of interest and I am particularly concerned about how it is going to affect small business.

You talk about it being an option. It seems to me it is something that is going to be done: it may not be optional. In my State such a proposal has already been filed. I think that we are going to have to gather information on the effect of measured service on small businesses and get it in a hurry.

If you have further information we would like to hear from you.

Mr. HIPP. In North Carolina, Congressman, we have had applications for optional local measured service on one-line service, residential or business on two occasions, and we have turned them down both times because of the opposition and because of the lack of data. But we have now installed in nine cities, or there is being installed, experimental, local measured service tariffs with different tariffs in each city. And Southern Bell has been ordered to provide data on who utilizes those tariffs and how cost-justified the tariffs are. We have not been able to find any material on the actual data support for LMS so far. So we are putting in this experiment in North Carolina.

Representative WYDEN. Mr. Chairman, I think this is something we ought to be looking at in greater detail because I share the views of the commissioner from Florida. You take the classic real estate firm with one or two people making a lot of calls, and I think if something is not done about these local measured service proposals, that small businesses could be very hard hit.

Chairman PACKWOOD. Well, again, I am not sure what we can do about them unless we want to preempt them.

Representative WYDEN. I think I, too, would be reluctant to preempt anything at this point. I think it is something we certainly ought to focus on because the large businesses are going to find it very attractive to bypass; the small ones are going to be off on their own.

I thank the Chairman.

Chairman PACKWOOD. Congressman Swift.

Representative SWIFT. Thank you, Mr. Chairman.

I would like to talk just a little bit about the lifeline service again.

How much of that do you have now in your States? Do you have a program where you have to sign people up or require telephone companies to offer lifeline service? Do you subsidize any people now? Do you have to actually make payments to poor people or in some way do something of a welfare nature so they can have phone service?

Mr. SCHNEIDEWIND. No.

Representative SWIFT. You do not do that in Michigan?

Do you do that in North Carolina?

Mr. HIPP. We do not have it in North Carolina other than a proposal for optional local measured service has been called a lifeline type of rate because it would offer a lower rate for those that wanted a lesser degree of service.

Representative SWIFT. How many people are involved in that?

Mr. HIPP. Well, we have had only one town that has had the local measured service any length of time, and only 8 percent of their customers have elected to use it, which we consider very small. It would hardly cover the second homes, I think, in that particular district.

We do not know why customers are using it, and that is the reason we have structured an experiment that will produce that data.

Representative **Swift**. My question then is this. We have had some very glib talk here today about how we are just going to go ahead and implement this program, and then we will set up some means of just handling this problem.

Do you have any idea of how great the new need for some kind of lifeline service, some kind of welfare program, how great that would be if we implemented this FCC policy, either that or just pull people off the system?

The bottom line, what they are really proposing here is go ahead with the FCC, and we will come back later and create a new welfare program.

Mr. **Schneidewind**. And the problem is that first of all we know in Michigan that of the people on public assistance, the State does not have enough money to have an additional $10 a month for telephones. So all of the existing people who are paying a $10 a month bill for regular unlimited service, sure, 700,000 families will shift over to the cheaper lifeline. But that money used to contribute will not be there. It will have to be added to everyone else. And then everybody who has a second home will certainly try to use it if it is not restricted.

Representative **Swift**. So we replace the system that we have now that is working fine, in which you do not have any significant welfare implications at all, people make those contributions to universal service, which benefits the middle income and the wealthy as well as the poor, and what we would replace that with is one in which revenues would be shifted very largely to large, large, large corporate users, primarily, and then we would institute a new welfare program, telephone stamps.

OK, now, if we did that, because it has been argued here, particularly by the gentleman from Massachusetts, that we could do that, and that would maintain universal service. Now, that is not my understanding of what universal service is. My understanding is that universal service is the concept that everybody's telephone is more valuable because they are connected to everybody else. A welfare program to replace universal service is a very different thing in concept and philosophically, is it not?

Mr. **Schneidewind**. And imagine the difficulties of trying to police it so that a person with a cottage in northern Michigan who is well to do is screened out from the person who lives next door who is living there and is unemployed or may be indigent but too proud to go in and ask for help. It creates an administrative nightmare that has largely frustrated States in their attempt to provide energy assistance on a targeted basis, if you will, other than just through the public assistance budget, you know. And in our State the budget money is not there.

So it is an administrative nightmare that sound goods in concept, but when you get down to try to do it, it is very expensive and hard to do.

Representative SWIFT. Well, it just seems to me if we want to adopt a policy and support the FCC in adopting a policy which has a massive economic shift from middle income and poor people to very wealthy business, fine. We should recognize that in so doing, however, we are also going to have to take the further step of creating an entirely brand new welfare program for people to fill in a hole that will have been created by what is virtually the elimination of universal service as we now know it.

I mean, we can go to something else and still call it universal service, but we will have lost what we have now and have had for four decades, and understood to be in fact universal service.

I thank you very much. It has been very helpful.

Chairman DINGELL. The Chair thanks the gentleman.

The Chair now recognizes Senator Lautenberg.

Senator LAUTENBERG. Thank you, Mr. Chairman. We are halfway through a vote. I would like very quickly to respond to the comment made earlier about the fact that some of the bills before us would simply preserve the status quo.

The fact of the matter is that Congress, I do not believe, ever voted for that status quo. That status quo developed as an administrative process because the monopoly in charge, the regulated monopoly, handled it that way. That was their business, notwithstanding that it was generally supported by reviews before the various PUC's.

Is that fair to say? I mean, Congress never did vote to distribute those revenues that way.

Am I correct?

Time is short. Yes or no?

Mr. HIPP. It is correct that Congress did not, but the state commissions did have a role in adopting and formulating those.

Senator LAUTENBERG. But the Congress never did and because of a change in circumstances this review is before Congress for the first time. So, in my view, it is quite proper to review the status quo and perhaps to make new arrangements because conditions are different.

Ms. RUDD. Senator Lautenberg.

Senator LAUTENBERG. I am going to keep the floor, Ms. Rudd. Perhaps you can speak to the chairman after I am gone, if you will forgive me. I do not mean to be rude. I am delighted to be here with you. But I do want to make one more comment before I rush off to vote.

The fact of the matter is that we must now make decisions based on totally changed demographics within our society, and a very significant aging population. My State is second to yours, Ms. Leisner, in terms of median age. New Jersey has the second highest median age in the country.

We are seeing many changes. I believe we have seen more people slip into the poverty class in this past year than we have seen in the last 20 years. So there are all kinds of new problems.

Therefore, I think it is quite appropriate to review how we distribute these telephones and who it is that we help. Simply because we had the subsidies before does not mean that we should not be looking at them or perhaps changing them.

I think that it is time to recognize that certain States that may be disadvantaged by a lack of natural resources, may also be advantaged, perhaps, by a low-cost efficient telephone operating system. Since they are forced to bear the disadvantages, perhaps they should enjoy the advantages.

Still, I am concerned that we retain universal service, meaning that everybody has a chance to have access. If you are concerned about administrative nightmares, Mr. Schneidewind, think of the nightmare of that aged person who is suddenly going to be in isolation because he or she cannot afford to communicate with a relative. I have heard things like suicide predicted, emotional distress, depression, etc. Those are the people that I am concerned about in my State and throughout this Nation. I am concerned about people who are job hunting and can only reach a prospective employer by telephone. I am concerned about a family in which a mother has to desert her children to go to work to earn a week's pay. I am concerned about that family. That is a hell of a nightmare, if you will forgive me, for someone not to be able to call up and say to the kids, are you OK? Those are the kinds of nightmares we as public servants are obliged to deal with.

So you will forgive the passion of my response, but I consider it a very serious and important issue.

And with regard to subsidized lifeline service, when we are selective, people are going to be attracted to the cheap service and they are going to take advantage and get lifeline for the bungalow or the vacation cottage or the second line. So, I think we ought to have a simple means test that is reasonable to administer. That is the obligation of our society, to see that we deal equitably with all of our people.

Thank you, Mr. Chairman. I am going to go vote.

Chairman Dingell. The Chair thanks the gentleman.

Under the rules, I think the gentleman from New York is entitled to be recognized.

Representative Lent. Thank you, Mr. Chairman.

I would like to just follow up on a question of the gentleman who questioned you previously, Mr. Swift, about the regulatory nightmare that might be imposed on, I assume, the telephone companies by providing some sort of a lifeline rate or base rate for the poor and the elderly and the indigent.

Actually, we have this service already pretty well in place in most States—I know we do in my State of New York. I assume in all of your States—a welfare system or social service system where people are either on welfare or they are not, and they are eligible for food stamps or they are not, or they are eligible for rental assistance or health care, medicaid, or they are not.

So I think that that perhaps is somewhat of a red herring, that we are going to have to create a whole new welfare system for telephone subscribers to determine whether or not they are eligible. Certainly it could be easily worked out by the local State governments using the existing system.

What I would be more concerned about in terms of a regulatory nightmare would be the regulatory nightmare that might well be created by the imposition of a bypass tax or a bypass fine on people who set up or firms that set up an alternative communication system. It would seem to me that this would place a tremendous bureaucratic burden on whoever is put in charge of collecting this fine or imposing this tax.

For example, we have not made any decision yet on what is a bypass. There are a lot of questions involved with that. How much should the tax be? Which user pays what tax?

So do you not see as well—and also the bureaucratic problem of making sure that those who owe the tax or the fine do not escape the tax. You have an enforcement problem.

Do you not see an equally great if not greater regulatory nightmare involved with this kind of a proposal of a bypass tax or bypass fine than you have with a system involving welfare where you already have the whole mechanism in place?

Mr. SCHNEIDEWIND. It srikes me, though, that right now the mechanisms being used, or proposed in both pieces of legislation, the Packwood approach and the Wirth-Dingell approach, have inherent in them the same relationship to what our business entity obviously is, the current taxation mechanism. Those are somewhat the same kind of obligations, and these companies also depend upon the telephone system as a backup to their bypass facilities without exception. Probably they are interconnected already, so there is a billing relationship. There are obviously far fewer of them in any given State in terms of numbers than there would be of the hundreds of thousands, if not millions of people in a State that would be eligible for lifeline.

So in terms of numbers of existing systems in place, it has got to be a lot easier.

Representative LENT. But if we set up this new regulatory mechanism, you think it would be easier to collect the bypass tax or to simply give a little old lady who is now on food stamps a stamp that she could use, one extra stamp, maybe she could use it to buy a telephone? You can buy a telephone, can you not, in Michigan, for $10 or $30?

Mr. SCHNEIDEWIND. I wish it was that simple.

Representative LENT. Let me ask this question because I think it is important.

If you gave a little old lady a $10 stamp in addition to her food stamps, she could buy a telephone, can she not, and avoid the $2 to $3 a month charge for renting a telephone that the Michigan Telephone Co. presently charges?

Mr. SCHNEIDEWIND. That is one idea.

Representative LENT. You could thereby——

Mr. SCHNEIDEWIND. Congressman, you asked me a question. Let me answer it.

The problem we have is that you have got a lot of people who are eligible for public assistance who are not on public assistance. You have got a lot, for instance, who become unemployed, and they may be temporarily on public assistance, and we have run up against this in the heating problem. Believe me, I speak from experience. And to try to find a mechanism that will screen their eligibility when they are not going to go on the regular welfare programs is hideously difficult. That is the problem.

Representative LENT. Commissioner, you used an analogy before, Penn Central, and that this is like Penn Central, and I would question that a little bit, about Penn Central's rates going up so high, because actually what happened with Penn Central is the ICC kept their rates so low that they could not provide adequate and reliable service, and there was a bypass that took effect. Shippers left the railroads and went to the barges, went to the truckers for a more adequate and reliable method.

I am really concerned with the problem of bypass here. I think that there are going to be literally thousands of large users that are going to leave the existing system and bypass it, and the local companies are going to lose these tremendous revenues.

We are going to hear later testimony from some of our major executives from telephone companies who are going to talk about how so few users of telephone service, long distance, pay such a large percentage of the overall cost. And when these people, when the E. F. Huttons and the Xeroxes leave the system, there are going to be fewer and fewer people left to pay for the costs.

Mr. SCHNEIDEWIND. I am concerned, as Chairman Dingell pointed out, what if a cable system comes into a local exchange and is wired up to 30 or 50 percent of the people and offers a chance for these people to all bypass residential? What we are doing by loading the costs on the residential customer is creating what is in the very near future a very attractive opportunity for all those people to bypass the local exchange.

Representative LENT. Exactly.

Mr. SCHNEIDEWIND. So by loading on the local customer, you are creating in them an opportunity to bypass and taking it away from another customer. And that is not a system that works.

Representative LENT. Commissioner, if you load up the costs that are associated with long-distance users in lieu of the access charges, which is the way these bills have handled the situation——

Mr. SCHNEIDEWIND. I am talking about loading up the exchange costs.

Representative LENT. You are going to provide a big incentive for those users who are presently supporting the system to go into bypass.

Mr. SCHNEIDEWIND. And create an incentive for the small user wired to a cable whose rates have been doubled or tripled to bypass the exchange via cable. I guess that is the main thing.

This approach of the FCC is too simplistic because it says let's keep one set of customers on by loading rates on the other. But those others are going to have their own bypass opportunities. So it is not a long-range solution. It is a short-range solution that ignores cable, and we cannot afford to accept it because then we will be back before you 5 years from now saying: hey, you have got to try to solve the problem because all those residential people are bypassing through the cable, and our exchange does not have enough revenue. That is a problem, too.

Representative LENT. Thank you, Mr. Chairman.

Chairman DINGELL. The Chair thanks the gentleman.

The Chair advises that there will be a vote on on the House floor in just a few minutes.

Chairman PACKWOOD. We can go right on.

Chairman DINGELL. I would like to express my personal thanks, and I am sure our chairman would do likewise, for your valuable assistance in these hearings.

Chairman PACKWOOD. You have been a most helpful panel. Thank you.

Let us move on, now, to our second panel: Andy Smith, Delbert Staley, John Clendenin, Raymond Smith, Donald Guinn, Ormand Wade, and John Hayes.

Why don't we wait just a minute until some of the crowd goes out. Can I ask those who are going to stay, to stay and be quiet, please? Otherwise, could you move out and close the door behind you so we can hear?

Andy, why don't you go right ahead. You are at the start of the list.

STATEMENTS OF ANDREW V. SMITH, PRESIDENT, PACIFIC NORTHWEST BELL; DELBERT C. STALEY, PRESIDENT, NEW YORK TELEPHONE; JOHN CLENDENIN, CHAIRMAN OF THE BOARD, SOUTHERN BELL TELEPHONE & TELEGRAPH CO.; RAYMOND T. SMITH, PRESIDENT, PENNSYLVANIA BELL TELEPHONE CO.; DONALD E. GUINN, CHAIRMAN OF THE BOARD, PACIFIC TELEPHONE & TELEGRAPH CO.; ORMAND J. WADE, PRESIDENT, ILLINOIS BELL TELEPHONE CO.; AND JOHN E. HAYES, VICE PRESIDENT, SOUTHWESTERN BELL TELEPHONE CO.

Mr. ANDREW SMITH. Mr. Chairman, if I may, I want to offer some comments on behalf of the entire group and I think that will save your time. At your request, we representatives of the seven regions have coordinated the subjects of our remarks to avoid redundancy and to highlight those areas of most prominent concern in the context of the some 13 bills that have been introduced to date on this subject.

I will personally discuss the overall topic of universal service and the objective, which we all share, to preserve and perpetuate it. Following my comments, Mr. Clendenin, who is the chairman of Southern Bell Telephone Co., and Mr. Staley, who is chairman of the New York Telephone Co. and CEO-designate of NYNEX, which includes New York and the New England company, will speak to the Federal Communications Access Charge Order 78-72. After these two gentlemen have chatted with you, I would then introduce the remaining topics to be covered by the other four regions.

It is not intended necessarily that comments of one region are reflective of the positions of the others, and this format has been designed only to avoid as best we can duplications of subject matter and not to suggest any philosophical unanimity.

The area that I represent, Mr. Chairman, includes several large metropolitan centers, but also is to a degree a rural area, with substantial sections sparsely populated. Incidentally, this is typical of the entire 14-State region served by U.S. West, our regional holding company.

Insuring that our customers have access to affordable telephone service, including a choice of options designed to fit their individual calling requirements and budgets, is one of our commitments. We share your desire that quality affordable phone service will continue to be available to the public.

As part of our effort to meet that objective, PNB has had optional measured service available for quite a time, and one of the options is priced as low as $3.50 a month, and this basic budget service is sometimes referred to in our territory as lifeline service.

We realize that some customers may not be able to afford even that lowest price optional service, and if it is determined that some additional degree of support is needed to cover the difference between the price of a given specific type of service and what it actually costs to provide that service, we strongly encourage a direct and targeted subsidy to the individual customer based on their need, as opposed to one that is dispersed in general or in a geographically related fashion.

If relief which may be necessary for some is not targeted, we have concern that the truly deserving may not receive an adequate level of support. We at PNB are actively involved at the State level in Washington.

There have been a lot of comments about studies to be made. We actually have one that has been made in Washington with the utilities and transportation commission, exploring the possibility of a locally administered universal service subsidy fund to provide direct assistance targeted to those who cannot afford, for one reason or another, basic telephone access.

This study of a possible targeted State universal service fund is part of a significantly larger effort on the part of the Washington commission to implement a State access charge environment similar to that contemplated under the FCC order. A study just released by the Washington commission on July 15—and I plan to enter that in the record, Mr. Chairman—demonstrates that in that State the highest premium flat rate service charged by any company in the State in 1984 will be $15. That includes an intrastate customer access charge and includes the $2 interstate charge that was commented on in the FCC order yesterday. No premium flat rate service in Washington in any telephone company will exceed $18 next year.

The commission in the State of Oregon is involved in a similar investigation. The detail is not yet available.

I appreciate that the legislative proposals you are reviewing will provide for an alternative to the subsidy mechanisms detailed in FCC docket 78-72 through a transitional reassignment of customer access charges to the long-distance carriers. These legislative proposals, if workable, would keep in place the subsidy now flowing to local telephone companies via the settlements process.

While I do believe that the basic theory underlying 78-72 provides an equitable and workable substitute to the traditional process, my initial reaction to yesterday's revision of 78-72 is one of real concern, deep concern both for the continued competitive capability of Centrex and for the obviously sharply increased incentive for bypass by AT&T, by other common carriers, and by large customers.

Chairman **Packwood**. Are you talking about their decision, their revised decision yesterday?

Mr. **Andrew Smith**. Yes, sir.

I am not philosophically opposed to a public policy decision that would assign costs in an alternative fashion, if that was necessary to maintain universal service. One critical point to remember is that, no matter how it is done, however, it is the customer ultimately who will pay.

Certainly, now more than ever, this issue of bypass must be dealt with, and thoroughly. We already have a large number of customers in the Pacific Northwest using their own networks.

Further complicating this problem is the fact that a high concentration of our long-distance revenue comes from a very small number of customers in a very few locations. We serve in PNB 99,900 business locations in Washington alone. If only 125 of those customers chose to bypass us, we would lose 20 percent of our long-distance revenues. This would equate to an immediate $3.14 burden on the monthly rate for all our customers to compensate.

We urge you, before legislation is enacted, to consider and evaluate some questions:

If a charge is approved for bypass users, how will it work? How will this plan, and what is its cost to be administered?

What level of charge for bypass users would be necessary? Who would enforce the reporting and the payment?

Consider the consequences of a large artificial subsidy burden being placed on firms such as Boeing that are competing in the international marketplace and supplying many jobs in our economy. If a fund is required to insure universal service, why not use the existing Federal excise tax as a starting point, or fund the subsidies by an excise tax on bypass equipment or use of the frequency spectrum, or through a tax on gross revenues of bypassers?

With public policy moving us into a fully competitive telecommunications environment, would a policy encouraging pricing unrelated to cost be inconsistent, unfair, and in the long-term disruptive?

How do we insure that those who really need financial assistance in paying their basic service bill get it?

These are just a few of the questions that occur to us and that are before the committee.

Our ability in the BOC's to continue offering quality, low-cost service depends on your decisions in these deliberations. We remain and offer our services as ready to work with you in any way possible as your review continues.

And, Mr. Chairman, I appreciate this opportunity to be here today. And incidentally, I will update my written testimony in line with the revision in 78–72 of yesterday.

Thank you.

[The statement follows:]

Statement of Andrew V. Smith on Behalf of U.S. West, Inc.

I appreciate the invitation of this joint committee to share some timely and important information with you today. I'm Andy Smith, president of Pacific Northwest Bell, one of the Bell operating companies. We serve customers in Washington, Oregon and a small portion of Idaho. My office is in Seattle.

I've been the chief executive officer of PNB since 1978. Prior to that I was the company's chief operating officer for eight years. Earlier, I was for five years PNB's vice president for the Oregon area. Our company serves approximately two and one-half million customers in our three State territory; an area which includes several large metropolitan centers, but also is to a great degree rural with substantial sections sparsely populated. Incidentally, this is typical of the entire 14 State region served by U.S. West which will be our holding company following divestiture. Along with PNB, Mountain Bell and Northwestern Bell provide service in those 14 States.

PNB has a reputation as a company concerned with the overall welfare and individual problems of the people of the northwest. PNB employees take an active role in a wide variety of local community activities and projects aimed at helping those who are elderly, disadvantaged or living on low incomes. During the past year, I was proud to represent all of our company's employees in special volunteerism award ceremonies—first in the White House with Mrs. Reagan and later in Governor Spellman's office in Olympia, Washington—when PNB received recognition for outstanding efforts to help the needy and less fortunate.

I assure you that PNB is sensitive to the needs of these groups, especially the elderly and those who live on low incomes. We will continue to be concerned about those problems in the years ahead also because PNB will be an active, involved corporate leader in the northwest. Insuring that our customers have access to affordable telephone service, including a choice of options designed to fit their individual calling requirements and budgets, is one of our commitments. We share your desire that quality, affordable phone service continue to be available to the public.

At PNB we're taking a number of steps already—and we'll continue to do so in the future—to keep affordable telephone service a reality. It makes very good business sense for us to work on this objective. Obviously, we want to sell our service to as many customers as possible. And, our customers will buy it if it has value. That value to a large extent is directly related to the ability to call anyone you need or want to.

Our determination to keep universal service a reality prompted us to establish an officer level group within a U.S. West some time ago to oversee our continuing efforts in this area.

Keeping phone service available and affordable is a big job. Insuring that we are ready to meet the service needs of new customers connecting to our network is also a major priority.

The concerns of Congress in this regard—which we share—are, however, only part of the overall management problem facing us. Inflation which continues to increase the cost of materials, labor and other operating expenses should not be overlooked. The cost of capital required to keep service working and satisfy subscriber growth requirements also adds severe pressure.

In our discussion of universal service I feel it is important to keep telephone rates, and any future increases in prices, in reasonable perspective. By any measure of comparison—the Consumer Price Index (CPI), various inflation indexes and so forth—the increase in the price of phone service has lagged far behind virtually every other product and service people use and consume. (See Exhibit No 1.) We're aggressively working on new innovative programs and rate plans to make sure that phone service remains affordable in the future.

Just a month ago, George Walker, PNB vice president for Washington-Idaho, testified before the House Select Committee on Aging's Subcomittee on Housing and Consumer Interests. Mr. Walker stressed some key points in reference to our company commitment to keep phone service available and priced fairly for all. For example, he submitted exhibits showing that:

The price of local phone service provided by PNB (1975–82) has gone up less than half the rate of increase in all other items on the CPI.

The price we charge today for home telephone service is less than half its actual cost. Seattle Premium residence service: Revenue $11.15 vs cost $25.00

The price for even premium flat rate phone service (our most expensive residence service) in Seattle represents only one percent of the monthly social security benefit received by an elderly couple. (See Exhibit No. 2.)

Our budget measured option takes less than one-half of one percent of that same monthly social security benefit. The price for this budget service is $3.50 in Seattle, for example, compared to the current $11.15 price for premium flat rate. (See Exhibit No. 3.) even if the highest level of access charges that PNB is considering are added to that $3.50 rate in 1984 it will reach only about $7.00. In addition to the budget option we also offer our customers a standard measured service option which is priced at $5.50, with $3.00 of usage included within that rate.

These lower priced options—which are full quality, 24 hour a day service with the price related to individual usage—are strong evidence of our determination to keep phone service readily available and affordable for all.

I'd like you to know also that we have made thousands of personal contacts with elderly and low income customers to inform them personally about these options. That effort is continuing. To illustrate customer acceptance of these measured service options, when we began active promotion of these services in 1982, some 6,653 of our residence customers had selected measured service. By the first of June 1983 that number had grown to 56,458.

We realize that some customers may not be able to afford even the very lowest priced optional service. If it is determined that some additional degree of support is needed to cover the difference between the price of a given specific grade of service and what it costs to provide that same service, we strongly encourage a direct and targeted subsidy to the individual customer based on need as opposed to one that is dispersed in a general or geographically related fashion.

If relief which may be necessary for some is not targeted, the truly deserving may not receive an adequate level of support. I include here those who by some geographical criteria are considered rural customers. Let me point out that some of those "rural" customers are large land owners or Californians who have vacation homes in the San Juan Islands in Washington State or in resort areas on the Oregon Coast. It is erroneous to conclude that all rural customers need a subsidy.

For those in a rural area where the cost of providing service may be higher—or for those anywhere who legitimately need assistance in paying for basic telephone access—we agree with Alfred Kahn, former chairman of the New York Public Service Commission and a past chairman of The Council for Wage and Price Stability. Mr. Kahn has expressed the view that the ideal subsidy from an economic and equity standpoint is a direct subsidy to people of limited means. He has stated, and I quote:

"This targeting of beneficiaries would minimize the burden on all subscribers—many of whom, too, are of very modest means—while at the same time ensuring that the benefits go only to the needy, and not, unfairly, to the people of ample means * * *. End of quote.

Mr. Kahn has addressed the issue clearly and has outlined a framework for dealing with this potential problem. It's workable and it's equitable.

In fact, we at PNB are actively involved at the State level in Washington to explore the possibility of a locally administered "universal service" subsidy fund to provide direct assistance to those who cannot afford basic telephone access.

Task force efforts have been underway involving consumers, telephone companies and the Washington Commission staff. The Washington Commission is undertaking public hearings throughout the State to determine the feasibility of direct aid to those who need assistance.

This study of a possible targeted State universal service fund is part of a larger effort of the Washington Commission to implement a State access charge environment similar to that contemplated for interstate services. A study just released by the Washington Commission, which reflects the July 27 revision of FCC Docket 78-72, demonstrates that the highest premium flat rate service charge by any telephone company in the State will be $14.95 in 1984, which includes an intrastate customer access charge. The vast majority of Washington citizens would pay even a lower rate—down to as little as $6.34. With the interstate customer access charge of $2 for residence customers in 1984, no premium flat rate service in Washington will exceed $17 in 1984. And, of course, budget measured service would be even lower still: in PNB about $7.

STATE OF WASHINGTON CURRENT RESIDENTIAL ONE PARTY FLAT SERVICE PLUS ESTIMATED 1984 INTRASTATE CUSTOMER LINE CHARGE

Company	1FR rate	Intrastate calculation	Total
Continental	$12.55	$2.63	$15.18
General	12.36	1.86	14.22
PNB	11.15	1.48	12.63
Mashell	7.10	4.48	11.58
St. Johns	6.00	5.24	11.24
Pioneer	7.00	3.96	10.96
Toledo	6.00	4.86	10.86
Western Wahkiakum	7.15	3.62	10.77
Tenino	6.00	4.30	10.30
Peninsula (Forks, Wash.)	8.74	2.61	11.35
Ellensburg	8.25	1.44	9.69
Hood Canal	6.50	3.06	9.56
Yelm	6.00	2.93	8.93

STATE OF WASHINGTON CURRENT RESIDENTIAL ONE PARTY FLAT SERVICE PLUS ESTIMATED 1984 INTRASTATE CUSTOMER LINE CHARGE—Continued

Company	1FR rate	Intrastate calculation	Total
Kalama	6.00	2.87	8.87
Lewis River	5.00	3.42	8.42
Telephone Utilities	6.10	2.16	8.26
Asotin	5.00	2.66	7.66
United	4.65	2.25	6.90

This unique State of Washington study is, I believe, the first factural analysis in the Nation of the precise effect on local rates of customer access charges.

Those of you from the Northwest may have seen a recent news clipping quoting Washington PUC Commissioner Mary Hall concluding after a review of this study that the Washington Commission was pleased to see how relatively low the required rates came out in the analysis, and that phone rates around the State won't jump nearly as high as many alarmists earlier estimated.

In fact, considering the concerns about unacceptable impacts on rural ratepayers being expressed, it's interesting that the Washington study shows that customers in the small rural community of Forks, Washington (population 3,060), which is served by the Penninsula Telephone Company, will still be able to get service at a rate less than that required for much larger metropolitan areas such as Seattle served by PNB and Everett served by GTE. Any conclusion that rates in rural areas may reach an unaffordable level is without any basis in fact in the Northwest.

Quite similar efforts to focus in on the real facts are taking place in Oregon also, involving the State commission, consumers and industry representatives.

Our business is rapidly becoming fully competitive. Over the past decade the FCC has aggressively implemented a series of policy changes to substitute competition in the marketplace for regulation. We have, and continue to, support this overall change in national policy. We are convinced that the public wants this and will benefit from an open competitive telecommunication marketplace.

I hope you share with me the view that our most critical task as we look ahead is to manage our way through this transition period and into the future with the advantages that open market competition brings and without the loss of universal service. I'm convinced that our rate plans, and other efforts at the State level such as I have described, and the access charge plan (FCC Docket 78-72), help that happen and are workable and fair. One concern I would express about yesterday's revisions in FCC Docket 78-72 is its treatment of Centrex. Damaging the competitive capability of this viable and profitable service will remove the contribution it has provided to local rates.

I appreciate that the legislative proposals you're reviewing would provide for an alternative to the sudsidy mechanisms detailed in FCC Docket 78-72 through a reassignment of customer access charges to the long distance carriers. These legislative proposals, if workable, would keep in place the subsidy now flowing to local telephone companies VIA the separations and settlements process. While I do believe that 78-72 has provided an equitable and workable substitute to this traditional process, I am not philosophically opposed to a public policy decision that would assign costs in an alternative fashion because we all agree on the desirability of universal service. The question is will it work. Uncertainty and quite a few critical questions fill my mind when I think about how any alternative subsidy program might be designed and made workable in a timely fashion. Certainly the issue of bypass must be dealth with thoroughly in any alternative proposals.

The FCC's proposal to phase in a customer access line charge also recognizes the very real and serious dangers of bypass. Let me briefly explain what "bypass" means in the context of long distance service and access charging and, more importantly, why we all need to be concerned about the real and negative consequences uneconomic bypass can cause.

First, I'll briefly define the two forms of bypass: economic bypass and uneconomic bypass. Economic bypass is in the public interest and is a natural condition in a competitive market. It occurs when differences in price are based on actual cost differences. On the other hand, uneconomic bypass occurs when differences in price are artificial because they are not—for whatever reason—directly related to actual costs. This situation ultimately is not in the public's best interest.

Customers who bypass—principally businesses—build a separate and alternative communications network which circumvents entirely the public long distance network and in some cases the local network too. Some of these firms also have the capacity to resell the use of their network to others. If the price of using the public network becomes an unattractive economic option for this type of customer, bypass becomes a viable alternative.

We already have a number of customers in the Pacific Northwest using their own networks. The U.S. Government, major newspapers and television stations, the Boeing Company, the Washington and Oregon State governments, Crown Zellerbach, and the cities of Portland, Seattle, Tacoma as well as Douglas County in Oregon are examples. Other companies and organizations no doubt will construct their own networks. Since many bypass systems now exist and have existed for years, I don't think it is practical or correct to try to prohibit them by legislation.

With bypass, access revenues are lost, forcing increased upward pressure on the rates for all othe customers. Ultimately, this situation creates a "death spiral" phenomenon because as prices escalate upward—due to large users leaving the public network and loss of that revenue—more and more customers opt for some form of bypass putting yet more of a support burden on those remaining.

Further complicating this problem is the fact that a high concentration of our long distance revenue comes from a very few business customers in a few locations.

We serve over 99,900 business locations in Washington alone. If only 125 of those customer locations chose to bypass—and they will if access charges are not levied on the cost causers fairly and phased in sensibly—we would lose 20 percent of our long distance revenues. This loss alone would equate to an immediate $3.14 burden on the monthly rate for all our customers to compensate for that lost contribution. That is simply not acceptable. In addition, these large businesses have told us they will not be agreeable to paying more than their fair share of these costs. A gradual phased in schedule which removes the existing subsidies over a number of years makes good sense to them and will minimize the bypass threat.

EFFECT OF BYPASS ON BASIC SUBSCRIBERS—WASHINGTON

Washington business MTS/WATS revenue	Number of business locations	Increase in monthly access line rate with bypass
10 percent	22	$1.57
20 percent	[1] 125	3.14
30 percent	367	4.71

[1] Represents 0.1 percent of the total 99,926 total business locations in Washington. If these locations were bypassed, subscriber monthly line rates would have to increase $3.14 to offset the contribution from the lost toll revenue.

I appreciate your recognition that to keep this subsidy in place requires that procedures must be carefully designed to insure that bypassers, including users of private systems, do contribute to the support of the local exchange network. The manner in which bypassers may be assessed charges and the design of an enforcement process, however, present enormously complex and unresolved problems which must be addressed and solved if the plan is to be fair and workable.

To summarize, we strongly believe—

Our current PNB plans, together with FCC Docket 78-72, are workable approaches to handling access charging and provide a mechanism that is critical to our economic viability, insure universal service and minimize the uneconomic bypass problem. Further, our local State efforts involving our State commissions, consumers and industry representatives will help us insure that the most equitable decisions for our local customers are made.

If some level of subsidy becomes necessary to defray part of the cost of basic service for individual, needy customers, we must assure that assistance is given directly to those who really need it and not administered with a broad general approach which will lead to unfairness, misuse and waste.

Our objective is to devote our best efforts—now and tomorrow—to make basic service available to the widest number of people. This just makes good business sense for us. New innovative service and pricing options will help us maintain that universal service reality.

PNB, and the other operating companies in U.S. West, are firmly committed to making this overall transition to the deregulated, competitive future workable. We are well down this transition road. Changing the rules outlined in FCC Docket 78-72 which have been carefully developed—with industry participation—over several years may result in chaos if the complexity and problems of alternative proposals are not dealt with in the very few months left before divestiture.

We appreciate your interest in taking a responsible look at these issues. Our fear, however, is that failure to address and solve the problems and unanswered questions in your proposals will lead to a chaotic situation in the industry that will threaten our viability.

We urge you—before any legislation is enacted—which modifies the intent and purpose of Docket 78-72 or changes the carefully planned overall divestiture process to consider and evaluate some questions:

If a charge of some type is approved for bypass users, how will it work?

What would this plan cost to administer?

What level of charge for bypass users would be necessary?

Who would enforce reporting and payment?

What are the consequences of a forced artificial subsidy burden being placed on large firms such as Boeing who are competing in the international marketplace? (General Motors, Weyerhaeuser, Techtronics are other examples.)

If a special fund is required to insure universal service, why not use the existing Federal excise tax as a starting point, or subsidies could be funded by an excise tax on bypasser's equipment, or use of the frequency spectrum, or a tax on their gross revenues.

With Federal regulatory and judicial decisions moving us into a fully competitive telecommunications environment, wouldn't a policy which would encourage pricing unrelated to costs be inconsistent, unfair and disruptive?

How do we insure that those who really need financial assistance in paying for basic phone service get it without a subsidy program specifically targeted to special qualifications such as disposable income or similar criteria?

Those are a few questions I leave with you. I appreciate this opportunity to be with you today, and I hope my comments have been useful to your review. Thank you.

EXHIBIT 1

The Price Of U.S. Consumer Products
Compared To Local Telephone Service
Percent Change, 1975-1982

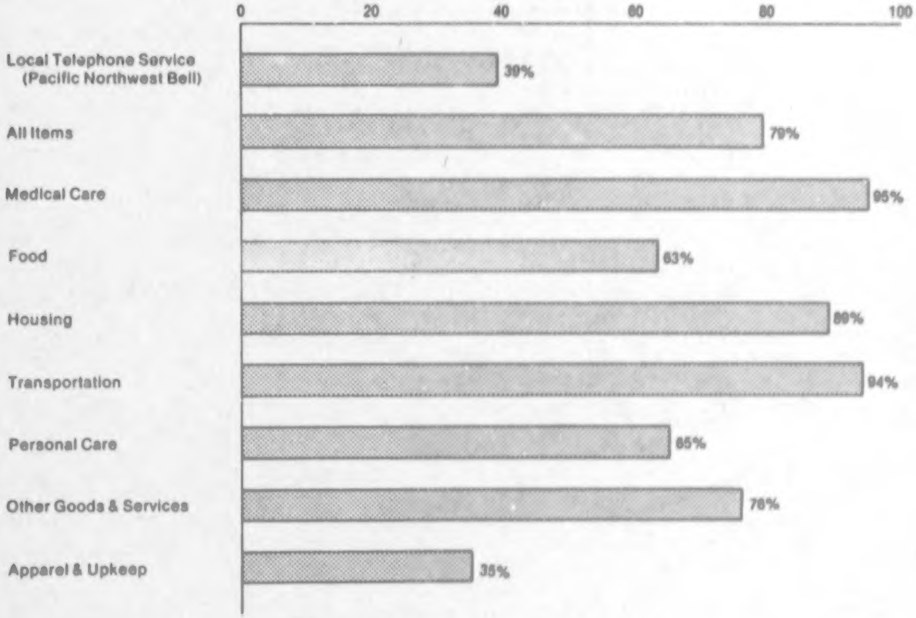
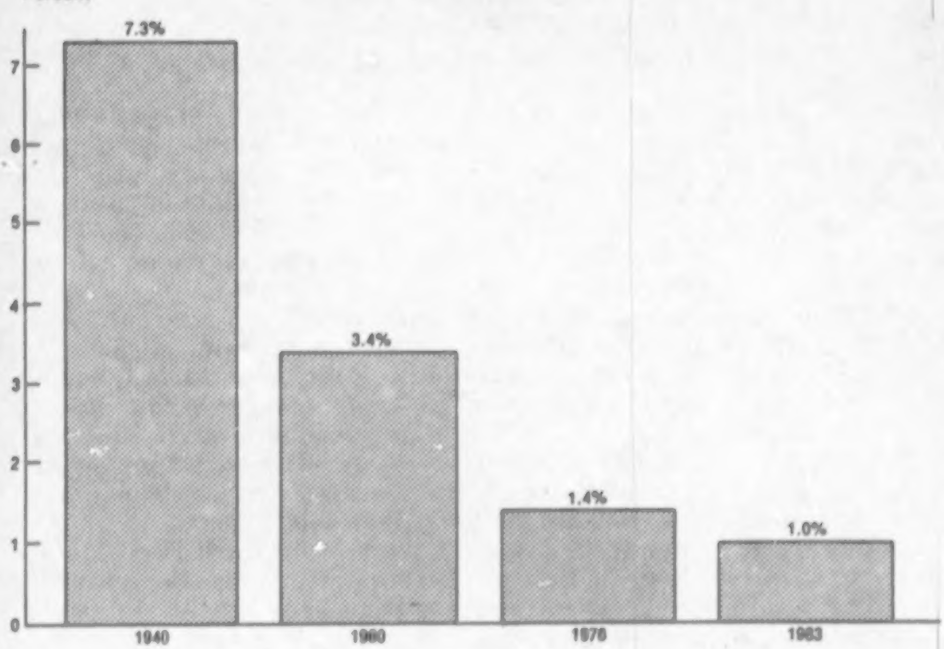


EXHIBIT 2

Monthly Residence Telephone Rate As Percent Of Monthly Social Security Benefits*

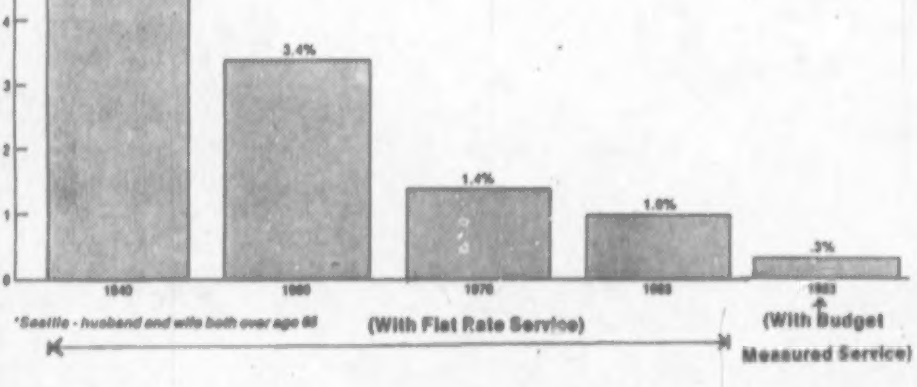


**Seattle - husband and wife both over age 65*

(With Flat Rate Service)

EXHIBIT 3

Monthly Residence Telephone Rate As Percent Of Monthly Social Security Benefits*



**Seattle - husband and wife both over age 65*

(With Flat Rate Service)

(With Budget Measured Service)

Chairman **Packwood**. Now, who do you want to go next?

Mr. **Andrew Smith**. Mr. Clendenin.

Mr. **Clendenin**. Chairman Dingell, Chairman Packwood, Members of Congress:

I am John Clendenin from Southern Bell. I welcome this opportunity to comment on the proposed legislation and I thank you for it. I commend both committees for the landmark nature of these joint hearings.

My written testimony aims at the seven or eight subjects suggested by some of your committee staff, so I shall not repeat that material now, but would be happy to respond to questions later.

Obviously paramount in all the legislative proposals is the concern over preservation of universal service at affordable rates. That is a concern we in Bell South and the Bell operating companies of the Southeast urgently share.

But to me it is indeed most regrettable that legislative solutions and guidance relative to universal service have been so long in coming, because the rules of this industry did not suddenly shift. The evolution toward competition in this industry began many years ago in both the Federal and State arenas, and has been accelerated by the availability of new technology. And with that evolution, the shift of subsidies which have served to keep telephone local service rates low became virtually inevitable.

In our great American economic system, competition drives prices toward true cost and there is no room left for a subsidy. If the Congress is now inclined to think that moving this industry toward competition was not such a good idea, it is indeed unfortunate that philosophical action was not taken several years ago, at least 5 years ago, to be precise, because that is when docket 78-72 got under way with its years of comprehensive deliberation.

But I personally believe it is too late to look back or turn the clock back. Competition is here. Bypass is here. Technology is exploding. We must look ahead.

And as the manager of a complex organization which has expended enormous effort to comply with the MFJ and the orders of the FCC, I was hopeful that we were finally close in docket 78-72 to having a workable set of industry signals. We badly need them.

As several of your committee members observed this morning, continued uncertainty is in itself a threat to universal service. There is an urgent need for final decisions.

But having said that, and before any precipitous action is taken to overturn or alter the 78-72 order, I urge extreme caution, because the access charges are absolutely essential to the preservation of universal service. Without them as a replacement for toll subsidies, the vitality of a company like mine and our ability to provide that universal service that you are so concerned about will vanish.

I personally feel——

Chairman PACKWOOD. Excuse me. Did you say without them as a substitute for toll service?

Mr. CLENDENIN. Without access charges as a substitute for the toll subsidies.

Chairman PACKWOOD. OK. I wanted to make sure I understood you.

Mr. CLENDENIN. I would be glad to repeat the entire sentence.

Chairman PACKWOOD. What you are saying is, if you do not have the access charges nor the toll charges, you cannot keep up the universal service?

Mr. CLENDENIN. That is exactly right.

And I personally feel that the notion, implied in some of the proposed legislation, that 78-72 in and of itself completely lost sight of the goal of universal service is an erroneous notion. I would remind you of several major features of the FCC's plan which are aimed at preserving universal service:

First, recognition of the economic reality of bypass. This required, among other things, replacement of the traditional usage-based recovery of non-usage-sensitive fixed subscriber access line costs. Over a several year transitional period, this completely unsound system of cost recovery will be replaced by direct recovery from the cost-causer, that is the access line subscriber.

Second, the setting of a gradual transition period toward full recovery of fixed subscriber access line costs, coupled with the building of a universal service fund and a monitoring plan, are safeguards erected to help assure optimum preservation of universal service. In connection with the monitoring plan, the FCC committed itself to action specifically aimed at protecting universal service.

Third, equitable treatment for all carriers. Equal access charges for equal access for all interexchange carriers to be achieved at the end of a 4-year phase-in, resulting in a truly competitive marketplace.

And fourth, lifeline service. Yes, included in 78-72! The FCC left this issue to the state PUC's, but it did provide for a waiver procedure under which an adjustment may be made in the amount of access charges applicable.

In my opinion, the access charge order provides as good a balance of interest and goals as could be expected or achieved with all the diverse interests involved. Nothing is perfect, but I believe the FCC's order provides a workable set of solutions, achieved after long and thoughtful consideration.

So while I applaud the intent of the proposed legislation to protect universal service, it is my judgment that the access charges proposed in 78-72, developed over years of public debate, are better suited toward the end of preserving universal service in the present competitive world of telecommunications than are many of the current legislative proposals.

Thank you.

[The statement follows:]

STATEMENT OF JOHN L. CLENDENIN ON BEHALF OF BELLSOUTH CORP., SOUTHERN BELL TELEPHONE & TELEGRAPH CO.; SOUTH CENTRAL BELL TELEPHONE CO.

My name is John L. Clendenin. I am Chairman of the Board of Southern Bell Telephone and Telegraph Company and Chief Operating Officer-Designate for the soon to be established BellSouth Corporation, which will own South Central Bell Telephone Company and Southern Bell Telephone Company following divestiture from AT&T.

I welcome this opportunity to appear before you today to express my views on behalf of the Companies of the Southeast Region regarding the legislation which has been proposed and to express our position with respect to several of the issues raised by the proposals.

Obviously, these hearings today are largely the result of concerns over the preservation of universal telephone service at affordable rates—concerns which we share. The bills before these Committees clearly are intended to help the industry continue with the provision of universal service. I would not want, therefore, to cast my testimony in terms of opposition to the purpose of the bills, but I question their timeliness and their approach to specifics.

There are many years of background behind us. We are finally close to having a workable set of industry signals, and I am frankly very concerned at the idea of yet another new direction and all the problems of working out its details.

As manager of a complex organization, I can tell you that a tremendous amount of work, and money, has gone into positioning the telephone industry to comply with the MFJ and the orders of the FCC. Further delays and further expense to the ratepayers are most undesirable.

For these reasons I would prefer to get on with the job under the rules we have. I hope we can continue to work with Congress so that the end result of any legislation can, in fact, achieve our common objectives with regard to universal service at affordable rates, and can do so with as little added expense and disruption of the industry as possible.

ACCESS CHARGES

Perhaps of greatest importance is the manner in which the legislation deals with access charges. The legislation proposes that access charges be paid entirely by the long distance companies or other persons that directly or indirectly interconnect with our local exchange facilities, as well as by private systems that do not interconnect. Since these access charges are the principal mechanism provided in the bills for preserving universal service and maintaining our financial viability, we fear that, if all the burden is placed on the carriers, there may be problems in obtaining the revenues required after divestiture to fully offset the loss of the toll subsidies which have been underpinning our exchange services.

In arriving at its decision in the access charge Docket 78-72, the FCC struck a realistic and workable balance among many conflicting interests and goals. In so doing, and in five years of comprehensive proceedings, a large number of consumers, businesses, customers, state regulators, government officials, other Common Carriers and established telephone companies, including AT&T and the Bell System companies, were active participants.

The major interests and goals the FCC sought to satisfy include these:

1. *Recognition of the economic reality of by-pass.*—This required, among other things, replacement of the traditional usage-based recovery of non-usage sensitive fixed subscriber access line costs. Over a five- to seven-year transitional period, this competitively unsound system of cost recovery would be replaced by direct recovery from the cost causer, that is, the access line subscriber.

2. *Maintenance of universal service.*—The transition period full recovery of fixed subscriber access line costs, coupled with the Universal Service Fund and monitoring of universal service, are safeguards erected to help assure optimum preservation of universal service. In this regard, the FCC is committed to a monitoring plan which would allow it to protect universal service. In the words of the Docket 78-72 order: "Such actions might include adjusting end user flat charges, adjusting the Universal Service Fund, adjusting the degree of nationwide pooling, or requiring that certain transitional benchmarks be met."

3. *Equitable treatment for all carriers.*—Equal access charges for equal access for all interexchange carriers will be achieved at the end of a four-year phase-in period resulting in a truly competitive marketplace for interexchange communications.

4. *Lifeline service.*—The FCC left this issue to the State PSC's by providing for a waiver procedure under which an adjustment may be made in the amount of the access charges applicable to such services.

In my opinion, the access charge order provides as good a balance of interests and goals as could have been expected or achieved. Nothing is perfect, but I believe the FCC's order provides a very fair and workable set of solutions, achieved after long and thoughtful consideration.

I would also like to add that I detect an excessive note of alarm in the debate on the merits of the access charge plan. Consider for a moment the fact that, on a national average, we are talking about reassigning less that $10 a month over a period of seven years to the actual cost causer. Consider the fact that many customers will see reductions in their telephone bill as a result of lower long distance charges. Consider the fact that during this same time period there should be, with the leadership and approval of state regulators, an increasing availability of local measured sevice options which will provide consumers a workable, practical opportunity for lower priced exchange services. Consider the fact that telephone set purchases will continue to offer the opportunity to reduce the monthly user charges they have experienced in the past.

So while I applaud the intent of the proposed legislation to protect universal service, it is my judgment that the access charges proposed in Docket 78-72, developed over years of public debate, are better suited to preserving universal service in the competitive world.

I have been impressed, however, with the clear understanding of the threat of Bypass expressed in the proposed legislation. In my mind, Bypass may be more of a threat to universal service than any other single factor, and to the extent that this legislation is attempting to solve that problem it is indeed working in the cause of universal service.

UNIVERSAL TELEPHONE SERVICE

Universal telephone service is a desirable social and economic goal. As the Chairman of a telephone company whose major business is and will be that of providing basic exchange service, it is certainly my personal goal to provide that service to as many customers as possible.

Let me cut to the heart of the question framed in this proceeding: "In the future, can the industry offer the consumer affordable access to the network which is responsive to his or her needs?"

My answer to that question is unqualified: We can and we will. Moreover we'll do it with the same ingenuity and dedication which has marked our people's efforts throughout the past 75 years since we, the industry, established the goal of universal service. This commitment has never been taken lightly.

Clearly, the transition of the past few years to today's competitive environment has posed some hurdles, but the industry overcame them and we'll manage the latest changes as we have those which came before, without sacrificing our commitment to the consumer. We'll do it in the future the same way we've done it in the past,—i.e., with the creative application of technology and service offerings which are responsive to the wide range of consumer needs. We now have, and, importantly, will continue to have, access to technology which will permit us to tailor our services to the needs of the business subscriber, the residence subscriber and the disadvantaged. Technology has permitted us to establish a productivity record four times greater than industry as a whole, and technology will continue to be fundamental to preservation of universal service.

Despite the spirited debate, I'm not convinced there is unanimity regarding the definition of universal service and I'm certain there is a range of opinions regarding what "affordable" means. I see this as something of a problem and would like to clarify where I am on these terms. The universal service that my industry has had as its objective is characterized by a reliable network, readily accessible to the consumer, which serves his essential health, safety, and basic welfare needs. The availability of telephone service which meets these needs should indeed be universal. This aspect of consumer well-being must not be trampled as our industry undergoes yet another transition.

It's equally important to recongnize those aspects of telephone service which should not be included in the definition of universal service. The achievement of universal service must not be measured by the opportunity for businesses to daily transmit for several hours and yet pay the same local rate as a shut-in who requires network access for medical reasons or to permit friends to check daily on his or her welfare. Any standard for universal service must *not* be designed to permit home computer owners to play a game of chess repeatedly and pay no more for their heavy usage than a person on a fixed income pays for his or her occasional usage.

We have in hand today technology which permits us to tailor service to meet the widely different needs of each of these consumer groups. We can relieve the occasional user of the cost burden imposed by the heavier user, deliver a measured service offering which meets his or her particular needs, and in the process keep the rate at least one-third lower than the average rate for unlimited service.

Proposals which would do this and meet the universal service standard are now pending in several states in the Southeast Region. I believe the cost realignments reflected in Docket 78-72 are essential and even when fully reflected in the proposals I've described will still produce access to the network which must be judged affordable. The daily price today of access to the network is generally less than an order of french fries, a bus ride, on a single-dip ice cream cone. As to prices tomorrow—I'm convinced our industry can continue its record of productivity increases, that the consumer will see significant decreases in charges for toll calls, and have available service which meets universal service standards at rates which by any reasonable measure must be judged affordable .

LEVEL PLAYING FIELD

The single most important principle which must guide any legislation that seeks to assure universal service while promoting competition is that all providers of local network services should be treated equally. Some systems should not be given competitive advantages over others simply because they are newer and may not, as yet, be as widespread, All competitors must be viewed as integral parts of a communications industry in rapid transition, and industry restructuring should be based on the existence of an equitable compeitive arena.

Disparate regulatory treatment which binds the telephone companies with regulation while leaving competing delivery systems free of the expense and delay of that regulation ultimately defeats the goals of universally available telephone service. Similarly, it runs counter to the notion of competition so often described in the last decade—that of fair, evenhanded competition on a level playing field. Disparate regulatory treatment tilts the field against the average ratepayer who bears the cost of providing the basic network for local universal service. Such treatment encourages bypass of the network through a variety of alternative technologies in ways that may be impossible to police or tax. The result will be that bypassers can avoid contributing to the cost of basic service.

It is not our position that any beneficial innovations in technology be artificially restrained. Nor do we argue that any particular segment of our industry, such as services provided by cable television companies, necessarily be totally regulated. But, we strongly believe that all participants in this business who offer competing, substitutable services should be treated the same with regard to those specific services. In the absence of such equitable treatment we might well find ourselves unable to respond to the needs of our customers. Not overnight, surely, but once an inequitable regulatory course is set for an industry where technological advances occur so very quickly as they do in ours, then it is just a matter of time before the residential, rural and business customers that unregulated competitors decline to serve begin to feel the adverse effects of a playing field tilted against them.

JURISDICTIONAL CONSIDERATIONS

There are two chief jurisdictional issues involved in the various legislative proposals.

First, certain of the proposed bills give the FCC exclusive jurisdiction over all long distance calls, including those which are entirely intrastate. They purport to do so in order to establish a uniform national policy.

I would simply point out that, historically, the state public service commissions have been a positive and innovative force in regulating our industry. The regulation of intrastate toll at the local level has worked well for a very long time. Moreover, it provides the state commissioners with an essential tool with which to fashion services and adjust charges to meet whatever unique circumstances may exist in different parts of the country.

Demographic, economic, geographic and other factors which impact regulatory considerations may clearly vary from one part of the country to another, and state regulation permits a direct, tailored response to those varying circumstances.

On the other hand, I recognize there are arguments for unified regulation of long distance.

The second jurisdictional issue addressed deals with the authority to set depreciation methods for local exchange facilities and for the portion of facilities used jointly for exchange and interexchange service.

Frankly, the critical problem our common carrier industry confronts is not jurisdictional so much as it is the absence of realistic action on the part of either Federal or state authorities to approve proper depreciation rates. We simply must be permitted to recover all our invested capital through depreciation at the rate that capital is consumed in providing service.

South Central Bell and Southern Bell are very capital intensive companies. It is absolutely essential to our continued viability in a competitive environment that the timing of capital recovery permit the retirement of obsolete plant. Failure to do so will undermine our past collective efforts to sustain a technologically efficient network.

In the past, under monopoly conditions, regulation delayed the recovery of capital—by prescribing long lives and using methodologies that did not match the capital recovery to capital consumption—in an effort to hold down rates. This was possible under the past monopoly environment when technology was evolving more slowly and competition was not a factor.

Even so, this postponement of capital recovery resulted in higher costs to our customers in the long run. For example, in the case of Southern Bell, studies indicate that 34 percent of our plant's useful life has been consumed. Yet only 16 percent of that investment has been recovered through depreciation expense. The adverse implications of such a policy are numerous. First, expenses incurred in the provision of service have been understated during the past period. This understatement continues today, and costs which should have been recognized in the past have been deferred to the future. Second, a higher level of investment remains in the rate base for an excessively long period, generating increased carrying charges. With straight line recovery, Southern Bell's annual revenue requirement would be $500M less today. Third, there is reduced availability of internally generated funds with which to finance construction, thus forcing additional acquisitions of new capital at prevailing rates in financial markets.

In a competitive environment, the undepreciated rate base has an adverse multiplier effect. Confronted with regulated prices that reflect a rate base inflated by inadequate depreciation, high-volume users will leave the regulated carrier and secure service from a lower priced firm that employs timely depreciation and newer technology. The average rate-payer then must pay the carrying charges on the entire rate base—that which he or she is using and that which would have served the high-volume user who took advantage of a competitive choice. With the undepreciated rate base producing regulated prices that are above the costs of new technology, high-volume users will refuse to pay them and the average ratepayer pays a bigger and bigger share of a larger and larger rate base.

Proposals now before our regulators will permit us to restore our reserve to reasonable levels in a 6-8 year period. During that period, we hope to reduce our rate base, in the Southern Bell example I cited, to a level some $4 billion lower than it would be under current policy. During these years, revenue requirements for depreciation would steadily decline. This decline would be an important offset to overall revenue needs at a time when upward rate pressure is continuing.

Before competition prevents it, it is imperative that the rate base be depreciated to reflect the current economic life of the assets. Because of past misperceptions about the function of depreciation, this is one of the critical turns in the road to full and fair competition. Only if we reach that point will the high-volume user stay with the regulated firm.

The real danger is that our failure to address adequate capital recovery will send our common carrier industry down the pathway of steel, textiles and autos versus worldwide competition.

The present joint state-federal process is addressing these problems and some progress is being made. But, I must add, not nearly enough.

We have urgent requests before the FCC now, and have likewise appealed to state regulators for help. Clearly, action is required and we're hopeful it will be forthcoming.

I would make one further point—whichever jurisdiction has authority—state or federal—or if new communications legislation is written—it is imperative that the common carrier companies in this country be given capital recovery comparable to the industry in which they compete.

PROVIDER OF LAST RESORT

Another issue currently under consideration is whether Congress should enable state public utility commissions to require all local telephone companies to continue to furnish basic telephone equipment and telephone wiring under tariff to residential and small business customers.

Implicit in this issue is the concern that customers may not be able to obtain these services, at a reasonable cost, except from a regulated telephone company.

Let me address this concern by first stating that I am absolutely convinced that the competitive marketplace has provided, and will continue to provide, numerous outlets for consumers and small businesses to obtain these services. This is evident in the fact that as of the end of 1982 there were already more than 21,000 retail outlets which sold telephones. These outlets include major department and specialty stores such as Sears, K-Mart, Radio Shack, etc. The number of those outlets increased 33% over 1981 and is increasingly rapidly each year. Additionally, catalog sales make the purchase and delivery of telephone equipment convenient for even the most remotely located subscribers.

Telephone wiring services are also readily available from a number of sources, including electrical and service contractors, telephone retailers, local entrepreneurs, and local telephone companies.

Given this environment, I believe the provision is unnecessary and will be of limited benefit. However, we do understand your concerns and those of your constituents and would offer no objection to the concept of a "provider of last resort", so long as the rates allowed us to recover all of our costs, including capital.

TRANSFER OF EMBEDDED BASE OF CPE TO AT&T

Several of the bills recently introduced suggest that the embedded base of customer premises equipment not be transferred to AT&T as currently required by the Plan of Reorganization. This legislation seeks to assign the embedded equipment base to the Bell Operating Telephone Companies on January 1, 1984. It appears that the intent of this change is to continue any subsidy now provided by customer premise equipment to local service rates. This provision assumes, however, that the embedded base contributes toward keeping down the cost of local service.

In fact, the amount of any subsidy realized for local rates is diminishing and competition will drive it to a minimal level. Indeed, retention of the embedded base by the BOC's could have the reverse effect of that contemplated by the proposed legislation. To date, all divestiture planning, including our plans to reenter the CPE market, have assumed the transfer of the embedded base to AT&T. A change at this late date would be disruptive to our employees and customers, as well as costly to our Company.

For these reasons, I believe that retention of the embedded equipment base in our companies would provide little advantage. In my opinion a far better answer would be the complete deregulation of all CPE, thus permitting all CPE, both embedded and new, to be treated alike.

Several of the bills would require the BOC's to set up fully separated subsidiaries through which to market customer premises equipment. It is difficult to understand why the divested Bell Operating Companies should be required to establish a separate subsidiary to market CPE when independent telephone companies are not required to do so. I am opposed to a fully separate subsidiary requirement since it would severely limit our options and in my opinion, make it very difficult for us to compete in the business. The current FCC Docket 83-115 deals with the separate subsidiary requirement. We have submitted comments in this Docket strongly urging that the separate subsidiary requirement be eliminated.

PROCUREMENT QUOTAS

At least one of the proposed bills also proposes to establish quotas which would control the quantity of products and services which we may purchase from Western Electric or Bell Laboratories. We do not believe that such legislation is beneficial or necessary.

The companies that comprise the Southeast Region are committed to seek out and buy technically suitable products and services at the lowest overall costs, regardless of the source. The continuing regulatory oversight we undergo, and the requirements which are part of the Modification of Final Judgment, should be more than adequate to monitor our performance. It is not appropriate to prejudge our actions by imposing quotas, but rather we believe that a post-review of our purchasing decisions will satisfy the critical concerns of you and your constituents.

LIFTING OF MFJ RESTRICTIONS

Under the terms of the Modified Final Judgment, the Bell Operating Companies are largely prohibited from providing any product or service after divestiture, beyond exchange telecommunications and exchange access service, that is not a natural monopoly service actually regulated by tariffs. The exceptions to this are the provision of certain directory services and the marketing of customer premises equipment.

While we do not welcome these limitations, we view the restrictions placed upon us as an inextricable part of the divestiture contemplated by the Modified Final Judgment. Consequently, we are prepared to abide by those restrictions until we are relieved from them on a case by case basis as provided in the Modified Final Judgment, or until they are removed through future legislative oversight.

CONCLUSION

In conclusion, I want to say again that this was a welcome opportunity to express my views on behalf of the BellSouth Corporation regarding the preservation of universal telephone service and the several related issues raised in proposed legislation. I hope I've been helpful.

Your interest and efforts on behalf of the companies I represent and our customers are sincerely appreciated. We have a common goal—that of continuing the best telephone service in the world and enhancing it so that we may all enjoy the extraordinary promise of the electronic information age.

Chairman **PACKWOOD**. Thank you.

Mr. Staley, are you going next?

Mr. **STALEY**. Yes, I am. Thank you, Chairman Packwood.

All of us here today want the same for the American phone user. We want good service, widely available, and at reasonable prices. We want, in short, precisely the same thing that Congress was concerned with obtaining for the American public in 1934, and that is universal service.

I very much appreciate being able to take part in these discussions. In my opinion, what is going on here today will be as decisive as what transpired in Congress nearly 50 years ago. Congress back then told the phone industry what it expected of it, but did not spell out how. Congress left the specifics to be decided by a remarkably broad Federal regulatory framework.

I doubt that Americans would have a versatile phone system today if Congress in 1934 had told the industry not only what it wanted, but how it wanted universal service to be obtained in highly specific terms. Yet that is what the two bills before this committee are designed to do.

Here are my specific misgivings to the two bills before this committee:

How can we insure that the needy have phone service? The answer provided by the proposed Senate bill is to expand the universal service fund which the FCC and the State regulators are in the process of establishing.

But this fund is a source of subsidy for high-cost, mostly rural, mostly small telephone companies. The targets, the recipients of the subsidy, are wrong. Not a single dollar of that subsidy would flow to the urban poor in New York.

The Senate bill would collect $100 million a year from New York State customers who make toll calls and give back only $6 million a year to largely subsidize New York rural telephone companies. In Massachusetts this amount is $25 million, with nothing being returned to Massachusetts. These rural companies will need financial support, no doubt. But does this really provide universal service?

What about the phone service for the needy in the cities of Boston, Detroit, Philadelphia, and other areas? These are the people which I believe the proposed legislation before this committee means to help, but does not.

What is more, the legislation in question I fear will endanger the financial viability of the Bell operating companies. This, instead of helping consumers, would jeopardize service to them.

We cannot wish away the costs of providing service. Those costs are there now and they will be there to be covered by us after divestiture, or everyone will suffer. The fact remains that New York Telephone and New England Telephone after divestiture from AT&T in 1984 will need almost $3 billion in revenues to cover the costs of providing access for long-distance calling. That amount represents more than one-third of our expected post-divestiture business.

I have said repeatedly that I am optimistic about the future of New York Telephone and New England Telephone. But I must say here and now that legislation which intends to scrap the FCC access plan would have severe financial impact on us and in turn on the service customers will receive.

Believe me, we recognize how hard it is to find an equitable solution to the access problem. For more than 5 years, the FCC has worked to develop a plan which it prescribed earlier this year. Virtually every segment of the industry and user group had a say in that plan. Indeed, I personally testified in the FCC open hearings.

It is a plan designed to be as fair as possible to all. It provides local telephone companies with a reasonable expectation of being compensated for the cost of providing access in 1984 and thereafter, and universal service will be maintained.

Bypass of the local network is another serious threat to low-cost service. This is recognized by the legislation in question and it is well that it is, for bypass is here. A whole industry dedicated to finding and exploiting bypass technology is doing a land office business. In New York City, the New York-New Jersey Port Authority, with Merrill Lynch and Western Union, are building a teleport to go around the local switched network. Cable TV facilities with access to satellites are in use in New York City.

The Senate bill before you proposes that a penalty be imposed on those who bypass us for the purpose of avoiding a user charge. That provision in my view is unworkable and unenforceable. The user under this bill would clearly be inspired to new heights to bypass us, for under the proposed Senate bill we would be asking the large users to pay $600 a month for what costs us $25 a month to deliver. Companies with today's technical ingenuity will not sit still for that, and the courts will not and should not stifle them in their use of new technology.

Indeed, the real deficiency of the Senate fine proposal is that it will stifle development and employment of American technology and at the very same time when we Americans need to encourage the development of such technology, for only with such encouraging signals from Congress will we maintain and in some areas regain our world leadership.

The House bill takes a somewhat different approach——

Chairman PACKWOOD. I am going to have to ask you to conclude your statement. We have got to hold the witnesses down to about 5 or 6 minutes.

Mr. STALEY. New York Telephone will very shortly propose to the New York State Public Service Commission a new form of lifeline service. That service will shield the needy and will be a targeted service. The FCC yesterday in its reconsideration order gave encouragement to that type of service.

Where do we go from here? I would like to urge this committee to be guided by the wisdom of the Communications Act of 1934. It created a framework for dealing with the very issues this committee faces. That legislation did not attempt to define the contours and limits of modern communications technology. It did not tell the phone companies how much to charge for service. It did not tell them how to deliver service.

It left those responsibilities to the industry and its regulators, and together we went on to build a communications capability for this nation the likes of which has not been seen anywhere. Let us preserve that framework. It is a flexible framework and it serves our nation very, very well.

Thank you very much.

[The statement follows:]

STATEMENT OF DELBERT C. STALEY, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, NEW YORK TELEPHONE CO.

Chairman Packwood, Chairman Dingell, and Members of both the Senate and House Committees, I am Bud Staley, Chairman and Chief Executive Officer of the New York Telephone Company, and the designated Chairman of NYNEX, the parent company of the New York and New England Telephone Companies after divestiture from AT&T.

Thank you for the invitation and opportunity to appear before this Committee and submit my views concerning the legislative proposals pertaining to access charges and the preservation of universal telephone service. Universal service has and continues to be a primary business objective of the New York and New England Companies. Moreover, the importance of access charges to the New York and New England Telephone Companies after divestiture cannot be overstated.

Universal telephone service developed in this country for primarily two reasons: (1) it was in the interest of the telephone industry to obtain as many subscribers as it could; and (2) Congress made affordable and universally available telephone service the objective of the 1934 Communications Act. While the telephone industry of today is much changed from 1934, nothing has occurred to alter these two objectives or place universal service in jeopardy. The same joint regulatory/industry framework that worked so well in the past to achieve universal service continues in place, and can be expected to further these same objectives in the future.

The continuation of universal service is, however, dependent on the financial strength and viability of the Bell Operating Companies after divestiture from AT&T. While I have been generally optimistic about the future of these companies, I am now concerned that passage of the recently proposed legislative efforts to scrap the FCC access plan could have severe adverse impacts on our future, and the universal availability of telephone service in this country.

In 1984, after divestiture from AT&T, the New York and New England companies will require almost $3 billion in revenues to recover the costs of providing access for long distance telecommunications services. This represents more than one-third of our anticipated post-divestiture business. The survival of these companies, and the continuation of our universally available high quality, efficient telephone system is thus largely dependent on our ability to recover these costs.

Earlier this year the FCC prescribed a plan of access charges that provides the local telephone companies with a reasonable expectation that they will in fact be compensated for the costs of providing access in 1984 and thereafter. The FCC plan took over five years to develop and took into consideration input from virtually every segment of the industry and user group. Because of the importance of access charges to the future of our Company, I was personally very involved in this effort and testified on behalf of the Bell Operating Companies at hearings held by the FCC.

The FCC plan is founded on basic and sound economic principles. The plan will encourage efficient and proper marketplace and investment decisions, and will foster technological advancement and innovation in the telecommunications industry. At the heart of the FCC plan is the concept of charging individual users of the telephone network based on the costs of providing service to these users. While in the past rates were established under a system of subsidizing basic rates with revenues from long distance rates, continuation of this subsidy in a competitive industry is not possible. Competition requires that prices be set based on costs.

The legislative proposals recognize the new problems posed by competition and the substantial threat to basic telephone service which could result through continuation of the historical subsidy approach. The proposals attempt to avoid this problem by levying a charge or tax on those who would by-pass the local network. These proposals are not, however, workable. They cannot be enforced and will leave the local companies with huge unrecovered costs, thereby severely impairing their ability to provide service.

The largest portion of the cost of providing access for either local or long distance service is the cost of the wire and associated equipment (the "local loop") which connects a subscriber's home or business to the local central office.

The monthly cost of providing this loop is the same whether the customer makes many or no calls, or whether all or none of these calls are long distance or local.

Under existing jurisdictional separations procedures, about one-third of the cost of this local loop is assigned to the interstate part of our business. These interstate costs are reflected in long distance rates and recovered from customers on the basis of the number and length of long distance calls made. The customer that makes no calls pays no part of this one-third of the cost of his local loop. The customer who makes many long distance calls may pay many times the cost of his local loop. We have many large business customers who pay $600 or more per month in usage charges to cover a service that costs us less than $25 per month to provide.

With the advent of new technologies and the introduction of competition, these larger customers are finding ways to avoid paying many times over the cost of providing service by turning to other services which by-pass the local network to complete their long distance calls. A whole new industry dedicated to finding and exploiting by-pass technologies and systems is now in its development. Just two of many examples of existing or planned by-pass in the New York City area are the Teleport being built by the NY-NJ Port Authority, Merrill Lynch and Western Union; and the use of Cable TV facilities to provide access to satellite facilities of other carriers. With existing technology, it is a simple matter to directly connect a large office building or industrial complex to the facilities of the interexchange carriers. Many such arrangements already exist.

The degree to which by-pass threatens the revenues of the New York and New England Telephone companies is no small matter. Because of the concentration of large banking, financial and other commercial institutions in our region, approximately one-third of 1 percent of our business customers provide us with one-third of our long distance related revenues, and only 5 percent of our customers provide us with approximately 70 percent of our long distance revenues. Thus, the loss of just a few of these largest customers to these by-pass alternatives can seriously effect our future business. This Committee must also understand that if we are to continue in business, the loss of revenues from these large users will have to be made up through increased charges for those customers who do not or cannot use by-pass alternatives; the very customers to whom universal service is so important.

The degree to which by-pass exists today is just the tip of the very large iceberg. Until now the largest interexchange carrier, AT&T, had no incentive to by-pass. That will change on January 1, 1984. After divestiture, it can be expected that AT&T will use its financial and technological resources to design and construct by-pass systems wherever this will provide it with competitive advantage. If it doesn't, its competitors surely will. When this occurs the drain on our revenues from by-pass systems will increase quickly and much more dramatically than in the past. Moreover, once customers and other carriers have committed themselves to by-pass systems, it will be too late to reverse the process by merely changing the system of access charges. After capital is committed to construct a by-pass system, a change in monthly charges is insufficient to cause a reversal of that decision.

The FCC access charge plan largely negates the problem of uneconomic by-pass by requiring that after a seven-year transition period the portion of local loop costs assigned to long distance services will be recovered directly from the subscriber using that loop. There will, of course, continue to be by-pass of the local network where others can provide local connections better or more cheaply than we can. This is what competition is all about, and provides a healthy incentive for us to find better and less expensive ways to provide access service.

All of the recent legislative proposals would totally scrap the access plan which took the FCC and the entire industry over five years to develop. In its place, these proposals would require that all costs of access for long distance service be recovered only from the long distance carriers. Since the long distance carriers must recover these costs from their customers, these proposals will continue the present system of over-recovery from large users—a system which provides incentives for large users and other carriers to by-pass our local network even where our costs of providing access are lower than theirs.

At least some of the recent legislative proposals I have seen recognize the reality of the threat and consequences of by-pass, and attempt to guard against the loss of revenues by requiring in one way or another that those who by-pass the local network continue to contribute to the cost of local telephone service. From the telephone company's point of view, these proposals that any provider of by-pass be required to contribute to local loop costs have some appeal. However, such a plan cannot work and, equally important, cannot be enforced.

The House proposal appears to require that a provider of a communication system that avoids using the local exchange network report his system to the exchange company in his area. It would then be incumbent on local exchange companies to file tariffs to treat such a by-pass provider as if he had used the local network. In order to develop an applicable tariff charge so that such a system would make an appropriate contribution to the costs of basic telephone service, a detailed analysis of the usage of by-pass customers would be required. This would require a by-pass company to provide sensitive proprietary information to its competitor, the local exchange company. Moreover, there is no way that a local exchange company could be assured that it has the information it needs from all by-pass companies. Furthermore, calculating appropriate charges would be extremely difficult, if not impossible. In many cases the by-pass system itself does not provide data as to usge. Therefore some arbitrary mechanism would have to be established to determine these charges. Such a mechanism would be a constant source of conflict. In short, such a system would require extensive records and regulatory mechanisms to ensure proper and accurate reporting of information to the local telephone company.

The Senate proposal is much more generalized in its approach. This proposal provides only for fines on those who by-pass the local network for the purpose of avoiding payment of access charges. Since the very purpose of by-pass is to avoid paying access charges, presumably all who use by-pass systems would be in violation. The proposal thus appears to outlaw all by-pass. However, in many, or even most cases, the $100,000 fine would be insufficient to prevent by-pass. The savings to a large user are often many times the amount of this fine. This propsal also does nothing to protect against the inevitable increased rates for the subscriber who cannot or does not use by-pass systems.

I have yet another and perhaps even more important concern with these proposals. Any approach which has assits ultimate objective or result the prevention of economically based by-pass systems would service only to stifle technological innovation and advancement. This is not in the long-term interest of either the telephone industry or the nation. We should all be trying to nurture and encourage the development and use of new technology. It is only through past innovation and development that it has been possible to bring high quality affordable telephone service into the reach of nearly everyone in this country. The future of universal service depends on continued advancements. Attempts to repress progress are doomed to failure.

If the proposed tax on by-pass systems doesn't work, the local companies will be faced with huge uncompensated costs which will threaten their viability and the future of our nation's telecommunications system. If I am wrong, and this tax on by-pass does work, the size of the charge would not only effectively halt by-pass, but would hinder the development of new systems which could be used by both local telephone companies and other carriers to provide more cost efficient access in the future. The risks attendant to this approach are just too great to chance.

The impetus for, and the goal of the legislative proposals is a perceived need to protect universal service during this time of change in the industry. This was also a goal of the FCC's five year effort to find a viable solution to the access charge problem. As the lengthy FCC proceeding demonstrates, the subject of access charges is a very complex matter requiring extensive analysis of the many changes currently taking place in the industry, and the competing objectives of the various interested parties. The wrong solution, such as those contained in the proposed bills, could have long term devastating effects, ultimately destroying the universally available and affordable system that now exists.

Under the FCC plan, end-user access charges will rise, and long distance rates are expected to decrease. Only the subscriber who makes few or no toll calls will see an increase in his overall bill. The FCC has stated its intention to monitor the effects of its access charge plan on universal service, and to make any changes which may be required if it appears that the imposition of end-user charges are forcing subscribers to forego service.

If indeed access charges do endanger universal service in any way, it is only those who truly cannot afford telephone service that are at risk. Protection for these customers is needed. In this regard, New York Telephone shortly will propose to the New York Public Service Commission a lifeline service. This service is directly targeted to the needy. To the maximum extent practical, it will shield the poor from price increases due to the access charge transition. To assure that only those in need are permitted to purchase this service, we will propose to the Commission a certification plan. Only those who are certified by a social agency as being needy may obtain this service. Thus an independent agency, not the telephone company will determine eligibility. This will avoid the problems of some customers subsidizing those who do not need a subsidy, such as the wealthy residential customer, those with second homes, etc.

We believe this plan is an appropriate response to the concerns about universal service. Other versions of lifeline service may be appropriate elsewhere, but we believe this plan is well suited to conditions in New York. No one need be denied service. At the same time, most customers will pay for the costs of the service they buy. We firmly believe that customers should get what they pay for, and it is not inappropriate that they be expected to pay for what they get. And, very importantly, the resulting costs of providing a subsidy to lifeline service will be kept in a range where they do not seriously impact our ability to do business, or threaten the future of the nation's telephone system. I believe a similiar FCC plan would be appropriate and could be accomplished within the parameters of the access charge plan adopted earlier this year. I suggest that Congress direct the FCC to develop such a lifeline access charge plan targeted to help the needy. I would be happy to work with both this Committee and the FCC to develop such a plan.

In the meantime, I urge you to leave intact the FCC plan. This plan, unlike the recent legislative proposals, provides the local telephone companies the means to recover the costs of providing access for long distance service and, to the maximum extent possible, ensures the future universal availability of quality telephone service. Any hurried attempt to change that plan at this late hour imposes major risks on the future viability of the local telephone companies and our nation's excellent telecommunications network. The regulatory framework that has existed for almost 50 years has served this country well—it has produced the best telephone system in the world with service rates that virtually everyone can afford. Given the chance, I am confident that the current system will continue to work and satisfy the legislative mandate of universal affordable service. Congress, of course, should continue its legislative oversight function. The wise approach is to implement the FCC's plan that so many of us worked so long to develop; see how that plan works; and then; only if necessary, require those changes necessary to assure the continuation of universal service as it exists today.

Thank you.

Chairman PACKWOOD. Thank you.

Mr. ANDREW SMITH. Mr. Chairman, in the following order: Ray Smith, president of Bell of Pennsylvania, will discuss recommendations or principles to guide development of legislation; and then Don Guinn, the chairman of Pacific Telephone, will discuss the general topics of competition, bypass, and local exchange franchise serving area considerations; following Don, Orm Wade, president of Illinois Bell, will discuss the issues of provider of last resort and fully separate subsidiaries; and then finally, John Hayes, vice president of Southwestern Bell, will discuss the topic of bypass.

Ray.

Mr. RAYMOND SMITH. Thank you, Mr. Chairman.

As the president of two telephone companies, I am also very worried about universal service. But I agree with my colleagues that the major threat to universal service is bypass of the local exchange and the resulting abandonment of investment and lost subsidy, not a customer access line charge.

Therefore, the solution to universal service problems is not to establish economic incentives to encourage bypass, but to provide low-cost options for all our customers. This method works and I have seen it.

In terms of bypass, less than 3 percent of our customers constitute 50 percent of the revenues and all of the profit. Just 200 customers make up half of the business income. And because of the current long distance subsidies, businesses are now laying plans to build separate networks which circumvent the exchange companies.

The rooftops of buildings are covered with microwave dishes and bypass is under way. If someone says that bypass is exaggerated, ask them about the "Washington Post," the Commonwealth of Virginia, Warner-Amex, Westinghouse, the AP, UPI, the Federal Government, or teleports in 16 of our largest cities. If we lost the revenues in Pennsylvania from just our top 100 customers, we would have to raise residential exchange rates by $4 a month.

The worst possible system is the one that we have now. It encourages bypass and it allocates costs unfairly. The FCC order would have improved that substantially. Yesterday they changed the order and it will require further study. Disadvantaging of the local company Centrex offerings, for example, is a major defect and must be corrected. Still, the original FCC approach was sound.

In terms of the bills before these committees, a few points:

First of all, if carriers and bypassers are to pay the costs, as some bills suggest, there must be a foolproof method to, as you, Senator Packwood, said, bring them into the system or charge them when they go off. This will require great fortitude on your part. Thousands of private systems have already been built. Congress, with a stroke of the pen, would be devaluing those investments. We will in effect as telephone companies be billing those people for services that we do not provide them, for services they do not want and they do not need.

However, if that is the intent of Congress, the following must be a part of any such solution: First, a specific method of identifying bypassers. Unless the exchange companies can identify them, they cannot bill them. Corporations, carriers, governments, and all other organizations will capitalize on any ambiguity to avoid the charges.

Second, a specific method of measuring bypass. Here again, the residential customer will pay the price of ambiguity.

Third, many of these bypassers will come to Congress for exemptions and they will be worthy objects of relief. But for the system to work, there must be a policy of no exceptions. If exceptions and appeals are permitted, the exceptions will quickly become the rule, and certainly governments, churches, newspapers, hard-pressed industries, wire services, social agencies, et cetera, will seek to avoid the charges. If exceptions are made, the local residential customer will pay for them.

Fourth, even if Congress can hold the line on exceptions, there will be a tremendous enforcement problem. The proposed fines are clearly inadequate. Those large users would pay them and then bypass, again the residential customer paying double or triple freight.

Fifth, assuming the problem of enforcement can be overcome, the difficulties of administration and fairness will still be substantial. Nationwide averaging will cause poverty-stricken residents of Newark to pay the telephone bills of millionaire ranchers out West. A new Federal bureaucracy will have to be created, imposing more rules and regulations on local companies, and unemployed steel workers in Pittsburg will be subsidizing Florida telephones. Certainly that person's $200 heating bills are not being subsidized by Floridians.

These are sticky problems that must be dealt with if the system is to work. It is a very challenging legislative checklist. With all due respect, I do not believe the pending bills calling for massive artificial subsidies solve the problems.

At the end of the line, though, even if all of these problems can be solved in the short run, the telephone companies will be artificially sheltered from the economics of the free market. We will survive by legislative fiat rather than as the result of inherent costs and the value of our services. What Congress decrees, it can rescind or amend.

In my view, the telephone companies should make their own way in commercial life. Their customers should pay for the facilities they use, and low-cost options that the FCC and some of our colleagues propose are the solutions to any universal service concerns. The FCC has produced a solution that needs some improvements, to be sure, but not abandonment.

Thank you very much.

Mr. GUINN. Chairman Packwood, I am Don Guinn, and so you will know the frame of reference of my remarks, I would remind you that I am chairman and chief executive officer of Pacific Telephone.

I appreciate the opportunity to participate in these joint hearings. I believe that telecommunications service is the glue that holds our society together.

The bills being considered in Congress address the preservation of universal service and certainly deserve very, very, very careful consideration. Universally available and affordable telephone service has historically been a fundamental goal of my company. We do not intend to abandon it. It will not be a relic of the changing times.

We agree with those in this hearing that have stated that the preservation of universal service requires some form of focused, lifeline subsidized service for the truly needy. We have provided lifeline service in our operating territory since 1968, and our rate plans for 1984 and beyond include the provision of a low-cost lifeline service for the truly needy.

At the same time, we do not believe that all residential users of telephone service need to be heavily subsidized. Most people can clearly pay a reasonable cost for local telephone service. I think we need to be discrete in who we try to protect as we preserve universal telephone service.

We believe the proper approach is to have an array of services. With a standard measured service, the service that most people would subscribe to. Have a lifeline service available for those who cannot afford standard measured service. And, to have a premium service which would be a one-party, free local calling service—that over time would not be subsidized—for those people who wish to purchase it. That way customers would have a full array of services to choose from that meet their individual needs.

We have filed rates according to that plan in our jurisdictions.

BYPASS

Some people would have you believe that bypass is something that is going to happen in the future, that it is not now a threat. Bypass is a threat, and it is not a future threat. It is here now and it is growing.

We recently employed the firm of Touche, Ross—and we will include their study in the record[1]—to study some 186 of our largest customers. What they found is, of these 186 customers, one-quarter bypasses today and one-quarter plan to bypass us in the near future. What they also found is that nearly two-thirds of the bypass facilities have been constructed since 1980, which is a measure of how fast bypass is growing.

In addition, here is another way of looking at bypass; 1 percent of our customer locations produce 33 percent of our message toll business revenue; and 1 percent produces 33 percent of the business toll revenue. If we were to lose that revenue, local rates would have to go up about $9 a month.

All of these customers tend to be concentrated in downtown urban areas. We have studied these customers and our studies show that for a fraction of what they will pay for access costs they could bypass us. In fact, many of them can bypass us for less than a penny per message unit, which is what they will pay through the carrier into the Universal Service Fund.

So bypass is here now, it is growing, it is a threat, and it is certainly a threat to universal service that needs to be dealt with very carefully as you pursue your deliberations on these bills.

Another area that I think needs careful attention is the local exchange franchise serving area. Congressman Dingell recently pointed out that the future of the local telephone distribution system is a crucial concern as we consider the issue of universal service. I agree with that completely.

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[1] The study has been retained in the committee files.

Fortunately, the California Public Utility Commission has recognized that concern and have held extensive public hearings on the issue of the local exchange franchise serving area, and whether or not intra-LATA competition should be permitted. I have argued before that forum that intra-LATA competition is contrary to the preservation of universal service. I would like to explain briefly why I have taken that position.

Today in California, Pacific Telephone realizes $700 million of subsidy from intra-LATA toll calls—not inter-LATA but intra-LATA—$700 million of subsidy. If competition is allowed into the LATA's and that subsidy is eroded, local rates in California would have to go up by an additional $8 a month beyond anything that has thus far been talked about in this forum today.

Also, that is probably not the worst effect of permitting intra-LATA competition. We would have to have rate deaveraging. Today we have averaged prices across the State. With rate deaveraging, prices would be driven to costs by competitive markets, and rates for local service would not go from $7—as they are today—to $29, which is our statewide average costs, but in Modesto they would go to $35; which is what basic service cost there. In Eureka they would go to our cost of $49, and in Baker, a small town near Palm Springs, they would go to $82.

The next thing that would happen is that the $23 that we now charge for local service connection would go to its cost of $145. Next we would have deaveraging by toll routes.

Unless the intra-LATA franchise service area is maintained, we are not going to be able to retain average pricing. We will not be able to avoid the increases I described, and as a result universal service to our suburban communities will be seriously threatened.

I would like to thank you for inviting me. As I said when I began, Pacific is committed to universal service and we stand ready to work with these two committees, with the Congress, with our regulators, and with others in the industry to preserve universal service.

[The statement follows:]

STATEMENT OF DONALD E. GUINN ON BEHALF OF PACIFIC TELEPHONE & TELEGRAPH

My name is Donald E. Guinn. I am chairman and chief executive officer of the Pacific Telephone & Telegraph Co.

Let me begin by saying that I appreciate the invitation to participate in the hearing of the Senate Committee on Commerce, Science and Transportation and the House Committee on Energy and Commerce.

I especially welcome the opportunity to comment on the subject of universal service, which seems to be at the heart of these legislative initiatives. Pacific Telephone is committed to providing universal telephone service at affordable prices.

Universally available and affordable telecommunications service has historically been a major goal of Pacific Telephone. We have not wavered from that goal in our 75-year history. And it remains firmly in our rate plans for 1984 and beyond.

I do not believe that universal service need be a casualty of the changes taking place in telecommunications today. But we do need to work together to ensure that universal service remains the hallmark of our Nation's telecommunications service.

My comments today will focus on a number of issues crucial to the maintenance of universal service in our changing telecommunications environment. I want especially to stress the measures we need to take to ensure the continuation of universally available, universally affordable telecommunications.

I define universal service as being connected to the network. That includes the dial tone necessary to place a call, the ability to receive an unlimited number of calls, prompt access to the operator, and 911 emergency services.

I'd like to take a minute to describe how Pacific Telephone has achieved its goal of universal service, and how we propose to maintain that goal in the new environment.

More than 94 percent of the households in California and Nevada have telephone service. Pacific—working with the California and Nevada Commissions—has achieved that goal by providing low priced basic telephone service to all subscribers. This tradition has not been and will not be abandoned.

It is important to keep in mind that the maintenance of universal service does not require that all local service be heavily subsidized. The great preponderance of customers can readily afford Standard Measured Service at the levels we have proposed—including appropriate state and interstate access charges. This type of service is a clear, economic bargain, as compared to other relative values. To preserve universally affordable telephone service we need to provide a low cost lifeline service that is carefully targeted for the needy. Our plan does that.

We currently have a rate case under review by the California Public Utilities Commission. In it, we proposed rate increases. At the same time we have proposed a rate structure that will enable all customers to obtain basic service at reasonable rates.

We have proposed that our Standard Measured service rate be increase from $3.75 per month to $7.50. Qualifying low income customers in exchanges which have Measured service will be able to subscribe to our Lifeline service for one-half the standard measured service rate, or $3.75.

We have also recommended that the rate for our premium flat rate telephone service—which includes unlimited local calling at no additional charge—be increased from $7 to $14.25 a month.

These rates do not include customer access charges which we have filed as $2.10 for intrastate and which we expect to be approximately $3.30 for interstate—except for Lifeline service which would have no intrastate and only a $1.00 interstate access charge.

In summary then, our proposed residence charges are:

	As filed with the CPUC	Access charges		Total
		Intra	Inter[1]	
Lifeline	$3.75	0	$1.00	$4.75
Standard measured	7.50	$2.10	3.30	12.90
Premium	14.25	2.10	3.30	19.65

[1] Tentative prices subject to further study.

Despite the presence of low cost options, we expect the majority of our subscribers—more than 75 percent in fact—to pay the higher rate for premium service because of the substantial value they attach to telephone service with unlimited local usage. But even at that higher rate, we'll be charging substantially less than it costs us to provide premium local service.

Since 1968, Pacific has offered Lifeline to its California customers, providing basic service to those with minimal local calling requirements. This measured service offering is available to more than 75 percent of our customers.

To ensure even wider availability of affordable telephone service to qualified low income people, we have proposed expanding our Lifeline offering to unmeasured exchanges at rates to exceed half the proposed charge for flat rate service with the same local usage availability. In these exchanges, where measured Lifeline service is not available, the increase for qualified Lifeline customers over current flat rate prices would be less than 50 cents. We believe these proposals will ensure that all of our residential customers have reasonably priced options available to them.

While we're proposing a substantial increase for premium service, we have to remember that basic rates in Pacific have been increased only moderately over the past 30 years.

For example, Pacific's premium flat rate service, which today is priced at $7 per month, was priced at $4.75 in 1950. If our price had increased at the same rate as the Consumer Price Index (CPI), we would now be changing well over $20 per month for this service.

But what we provide to that person for $7 per month costs us on a statewide average about $29. That's more than four times what we charge today.

Universal service has made an incalculable contribution to the social, economic and political well-being of this nation. Pacific believes in universal service. As you address this issue, I pledge that we will work with you in a spirit of cooperation and mutual concern to help design alternatives. But we must proceed with caution as we examine alternative ways to reach our common goal. Hastily made decisions, or the rejection of a workable mechanism like the access charge plan outlined in Docket 78-72, could damage the very goals we're trying to attain.

With this mind, I want to discuss a number of issues which touch closely on universal service.

THE FCC ACCESS CHARGE ORDER

The FCC's access charge order in Docket 78-72 provides guidelines for the establishment of access charges. These charges are designed to replace the subsidies local exchange service has received from long distance.

The order requires that a significant portion of end user non-traffic sensitive (NTS) access costs be shifted from long distance carriers to local customers.

Pacific supports the provisions of 78-72 because we believe it is the best proposal advanced so far and provides a reasonable balance between the needs of local customers, exchange carriers, and interexchange carriers. As long as a subsidized Lifeline service is available, we believe that the orderly shift of end user NTS access line revenue requirements to the customer through a flat rate charge will have a minimal effect on universal service. It will also provide necessary and realistic safeguards against bypass.

While the FCC guidelines are a major step toward these goals, I believe that low income customers need some special treatment to insure they remain on the network.

Consequently, in our California access charge filing of June 30, 1983, Pacific proposed that no state access charges be included in Lifeline rates. In addition Pacific plans to petition the FCC to waive the portion of its order which requires a minimum $2 per month interstate access charge for each residential customer. If this request is approved, Pacific's Lifeline rate will be only $4.75 a month, including a $1 interstate access charge, but no intrastate access charge.

The competitive environment in which we do business today will allow us to preserve universal service only by reaching a difficult balance between the ability of low-income customers to pay, and the economic incentive for large customer to bypass Pacific's network.

Any modification of the FCC order, or any legislative action to override its provisions, must provide realistic protection against bypass. The protection should be at least equal to, or preferably greater than, what has been provided by the FCC and it must be sustainable over time.

Any modification or override must also be adminstratively prudent. That is, it must regulatory agencies and local exchange companies with the flexibility to respond quickly when universal service is threatened by developments within the industry.

As I have said, Pacific supports the provisions of the FCC Order in Docket 78-72 as the best solution offered to date. At the same time we stand ready to work with you to design provisions which will strengthen universal service, prevent bypass and insure the viability of the local exchange companies. This is a complex undertaking that needs to be carefully considered.

UNIVERSAL SERVICE MECHANISM

Keeping local rates affordable is the key to preserving universal service. I believe it is possible to set prices which simultaneously meet universal service objectives and protect the revenues of the local exchange companies. Some of the principles that should guide this mechanism are:

Prices should not provide an incentive to bypass.—If the price burden on heavy users of long distance significantly exceeds the cost of other alternatives, they will bypass our network. The revenues lost from bypass will cause local service rates to increase, putting additional rate pressure on those customers which remain on the network. This in turn will cause more customers to leave the network, the fixed costs remain and additional increases would be required . . . thus creating a vicious cycle.

The irony is this: If we unduly burden heavy users in order to protect customers' basic sevice needs, we will ultimately cause higher prices for those customers we wish to protect.

Our goal, therefore, must be balancing the cost burden between heavy and basic users so as to keep long term prices at the lowest possible levels for all.

Bypassers should help support the cost of local service.—The importance of bypass is demonstrated by the proposed language included in H.R. 3522, which would prohibit bypass.

"In the adminstration of this act, the commission shall issue such rules and regulations as may be necessary to assure that all telecommunications services provided by an interexchange carrier certified by the commisson shall originate and terminate over the facilities of a local exchange common carrier".

Bypass is a critical issue that is further emphasized as a result of the concentration of long distance usage. For example, 1 percent of Pacific's business locations generate approximately one-third of all business long distance revenues.

If bypass is to be permitted, it is appropriate to require those who bypass the network to assist in the cost recovery of local exchange service.

However, such a subsidy must be administratively feasible. Relying heavily on bypassers for revenue will prove extremely risky unless a viable plan can be developed. We need to be certain that any alternatives provide equal or better bypass protection than that provided in the FCC Order.

We should provide a targeted lifeline rate.—Affordable service means different things to different people. Obviously, a person's income level has a lot to do with how one defines it.

As a general rule, I believe local telephone service in our operating territory is an economic bargain and most people can afford it.

Our commitment to universal service means we must be concerned with those relatively few customers who simply cannot afford to pay the full cost of basic local service.

In California, Pacific has filed a Lifeline rate that protects customers most vulnerable to price increases. But if we're to keep the rate low—$4.75 a month—we believe it is necessary to target Lifeline service to those for whom it is solely intended—low income customers.

UNIVERSAL SERVICE FUND

We are in support of the Universal Service Fund concept. As the price of local service moves toward cost, we're concerned about areas where the cost of providing service is well above the national average.

Federal and state commissions have formed a joint board to devise plans for keeping rates in high cost areas affordable. Out of those efforts have come a proposal which I believe provides a workable solution to that problem.

Briefly, the proposal provides a subsidy to areas where costs exceed 115 percent of the national average. This subsidy is paid for by a national surcharge on calls made through the interexchange carriers such as AT&T, MCI, and Sprint.

This plan is designed to keep service affordable in high cost areas without unreasonably burdening customers which provide the subsidy.

As I have previously stated it is important that this mechanism be designed to minimize any incentive to bypass.

COMPETITION WITHIN THE LOCAL EXCHANGE

If we are to maintain universal service, we must pay careful attention to the question of competition within the LATAs, or Local Access and Transport Areas.

The LATA concept called for in the Consent Decree and approved by Judge Greene provides a common, consistent approach to defining the local exchange company's operating territory.

With respect to that operating territory, I testified before the California Commission—and continue to maintain—that intraLATA competition in local markets will undermine our goal of preserving affordable, universal service.

I'll illustrate my point with figures I presented to the California Commission. Today, local service in California receives a subsidy from intraLATA long distance of $700 million a year. For every $85 million of this revenue we lose to competition, local rates must increase $1 per month.

That's why competition within the LATAs would inevitably drive rates to cost. We would lose the ability to maintain a subsidy to basic service. Based on the current annual subsidy of $700 million, the effect on our customers would be an additional increase in the basic rate of about $8.00 per month. I do not believe that there are any offsetting benefits to be gained from intraLATA competition.

There is an even more significant problem—the impact of competition on rate averaging. Deaveraged local rates—caused by intraLATA competition—would dramatically impact a sizable number of customers. As an example, let me cite the costs of providing service in some California cities. The cost in San Francisco is $26 but escalates dramatically as we move away from urban centers. Modesto, for example, is $35. Yeka, $49. And Baker, in the Southern California desert, is $82. An intraLATA franchised serving area must be maintained if we are to sustain average pricing and avoid the increases described above.

STATE-FEDERAL JURISDICTION

I would like to comment briefly on some of the jurisdictional issues which have come before you.

The first of these is depreciation.

Quite simply, I believe that state commissions should have the authority to establish depreciation rates for equipment used to provide service within their states. However, I also believe that some federal guidelines are necessary to ensure that states authorize adequate capital recovery. Let me explain why.

Accelerating competitive and technological developments are drastically shortening the projected life of Pacific's plant. Capital recovery must be adjusted to recognize these market place realities because adequate capital recovery is critical to our financial viability.

On a true straight line depreciation basis, Pacific should have recovered twice the amount of its invested capital repaid to date * * * approximately 40 percent instead of the 18 percent actually recovered. The low level of recovery results from depreciation methodologies founded in the monopoly era which reflect slower technological changes and which are seriously out-of-date today.

If we adjust for differing ages of plant assets, other information services companies have recovered 40 percent or more of their invested capital. To be competitive and efficient Pacific must be treated like the rest of the industry.

Pacific needs depreciation schedules which match capital recovery to the new telecommunications marketplace and advancing technology so the rate payer of the future will not be burdened with costs that should be paid today. We would welcome the opportunity to participate in the development of any guidelines related to depreciation.

The second jurisdictional issue is whether or not there should be a Carrier of Last Resort. I do not believe that California and Nevada need a "carrier of last resort" to provide a telephone instrument and basic wiring.

I say that because telephones are widely available throughout the areas we serve, and are also available through mail order catalogs. Prices for basic telephones are very low. And people who wish to do so can install inside wiring themselves or contract to have it installed.

However, I believe that it is appropriate for state commissions (as opposed to federal) to have the authority to decide whether or not exchange carriers should provide and maintain a single telephone and the associated inside wiring, if requested by the customer. Any such program should provide that the costs for these services be fully recovered by the prices charged for them. We believe it is appropriate for us to work with the California and Nevada commissions to resolve the "carrier of last resort" issue.

CATV—S. 66

I'd also like to point out our strong opposition to the provisions of S. 66 which would deregulate CATV providers, allowing them entry into telecommunication markets while we remain unable to compete effectively. In other proceedings we have argued that:

Pacific's current pricing structure is burdened with subsidies that would make immediate repricing to meet competition difficult, if not impossible.

The threat to universal service is real when revenue used to subsidize basic telephone service is eroded by unregulated competition.

While CATV is allowed to compete, it is not required to offer universal service, nor to provide any subsidies. Further, the CATV industry would be allowed to set its rates without any administrative review to protect the public interest.

This can have only one effect. We will lose to these firms highly profitable, heavily used routes which we rely on today to subsidize basic service. That's why I believe such legislation is not consistent with our universal service objectives.

BYPASS

Bypass is not just a future threat; it is a serious current reality.

A study conducted for Pacific by Touche, Ross in June, 1983 sought to guage the impact of bypass on our 186 largest customers. The survey concluded that: one-fourth bypass today; one-fourth plan to bypass in the next three years; one-fourth are undecided about bypass; and one-fourth will not bypass, have not decided what to do, or did not respond.

Customers bypass the local network in two ways—either by building their own network, or by directly connecting to an interexchange carrier's network.

There are over 4,300 private microwave channels operating in California.

Also, of the 675 satellite earth stations in California, about 250 are used for telecommunications. None of these belongs to Pacific, and one belongs to AT&T.

Today we have no data on the extent of interexchange carrier bypass in California. But we do know that Pacific provides about 58,000 dedicated access facilities to connect customers with interexchange carriers. Customers with these facilities, as well as those who use WATS and 800 services, are prime candidates for bypass.

Another bypass threat is the teleport, a hybrid of private and interexchange carrier bypass. A California developer recently announced its intention to build such a facility in the San Francisco Bay Area. It will contain six satellite earth stations, and be linked by fiber optic trunks to San Francisco and Oakland.

Crucial to the question of bypass is the price our customers pay. Any usage price which reflects non-traffic sensitive costs places an uneconomic burden on them. The greater that burden, the greater the incentive for them to leave the local network.

This is particularly true for our largest customers, who are concentrated in downtown areas. Our studies show that many of these customers could build their own bypass system at a fraction of the proposed access charges.

Should they leave, we will have no alternative but to recover the remaining costs from our residence and smaller business customers. This would be a significant threat to universal service.

PROCUREMENT

One issue particularly onerous that has been discussed in pending legislation concerns procurement. Specifically, the proposed legislation requires that within three years of their divestiture, the operating companies must purchase at least 8 percent of their requirements in any product category from manufacturers unaffiliated with a dominant carrier. This percentage woud increase annually until operating companies procure 30 percent of their requirements from unaffiliated manufacturers.

These provisions seem unreasonable and will work to the deteriment of the operating companies and their rate payers. Pacific plans to buy large quantities of equipment and supplies from a wide variety of companies. We believe the other BOC's will as well.

Legislative attempts to force-feed competitors into markets are unnecessary and will place operating companies at a disadvantage in negotiations.

CONCLUSION

Let me conclude by reiterating my confidence that universal telephone service need not become a relic in today's telecommunications environment.

We have given this subject our highest priority in California and Nevada. We have taken positive actions before the California and Nevada Commissions to preserve it. We intend to do likewise before the FCC. And we have pledged ourselves to assist you in your deliberations in any way we can. It is a critical issue. Critical to you, critical to us, but, most importantly, critical to our customers, who depend on universal telephone service for their welfare and their livelihood.

At the same time, as we pursue that goal we must proceed cautiously. Universal service is a complex issue—easy to advocate, but difficult to implement. The telecommunications industry is evolving rapidly. Bypass is here today and is a serious threat to the exchange companies for the future. We cannot assume that we know all the changes that could affect our ability to provide universal service. A fundamental requirement of any universal service proposal is that the local exchange companies and the regulatory agencies are afforded the flexibility they need to respond to changes as they occur in the telecommunications environment.

Thank you again for this opportunity to testify at this hearing. I can only say once again that Pacific Telephone is committed to universal telephone service and stands ready to work with you, with our regulatory agencies, and with others in the industry to preserve it.

Chairman **Packwood**. Thank you.

Mr. **Wade**. Chairman Packwood, members of the committee, I too appreciate the opportunity to appear before you today as we address these matters. They are really of great significance to our industry.

Illinois Bell is one of the five soon-to-be-divested telephone companies in the Midwest which will become a part of the regional holding company known as Ameritech, American Information Technologies Corp.

Competition and deregulation in telecommunications have reached the stage where it is appropriate to take stock. The plan of reorganization and for divestiture of the Bell operating companies is clearly very far along. The FCC and State regulators have taken steps to adapt the regulatory framework to the forces of competition.

Today, we are considering bills intended, at least in part, to preserve universal service, a goal that I strongly support. Our review, however, suggests that permanent solutions are being fashioned before the nature of the problems to be solved is clear.

In my brief presentation, I will address two topics: The concept of provider-of-last-resort, and separated subsidiary requirements for the Bell operating companies. While these are significant matters, I must emphasize that the questions of universal telephone service and access charges are of paramount and transcending importance in the legislative proposals that you have before you. Those issues are dealt with in a separate written statement which I have filed on behalf of Ameritech.

The concept of provider-of-last-resort, as contained in H.R. 3621, is that the local telephone company may be required to provide a basic telephone instrument and associated inside wiring on a tariff basis. The intention is understandable.

The difficulty is singling out unnecessarily and burdening, again unnecessarily, a single supplier in a highly competitive market. That result is antithetical to the development of a competitive marketplace. It is at odds with the objectives of deregulating competitive markets.

Most of all, however, the provisions are unnecessary. Today, one can obtain from any number of retail outlets or mail-order houses a telephone instrument for less than $20; as Congressman Markey observed a little earlier, $10 in this morning's paper. Wiring and jacks are equally available.

In short, I do not believe that the problem sought to be resolved by the provider-of-last-resort feature actually exists.

However, if Congress believes that a problem may exist in some specific areas over the next few years, the provider-of-last-resort concept should be tailored to that limited situation, and any such provision should be limited to areas and time periods where competitive alternatives do not exist and should mandate that charges for any equipment or inside wire established by the State commissions be fully compensatory, including the cost of maintenance.

Under existing FCC rules, this could be accomplished simply by removing from the Bell operating companies the requirement that they provide terminal equipment through a separate subsidiary. The FCC rules already permit States to compel non-Bell companies to provide such equipment on a provider-of-last-resort basis where competitive alternatives are not readily available.

Moving to the subject of separated subsidiaries, the various proposals would in my judgment make it more difficult to provide equipment to our customers. Neither S. 1660 nor H.R. 3621 proposes that a separate subsidiary be required in order for a Bell company to provide telephone equipment to its customers. Several other bills introduced in this session do, however, propose just that.

Legislatively imposing these requirements is unwarranted and unwise. After careful review of the extensive record on competitive markets in terminal equipment, Judge Greene in his opinion approving the divestiture declined to impose a separate subsidiary requirement on the divested Bell companies.

The FCC is considering whether its existing separate subsidiary requirements should apply to the divested companies. The Bell operating companies' comments in that proceeding detail the reasons that this is unnecessary; it is a cost burden and is unsound policy.

Legislation requiring a separate subsidiary would surely not be beneficial to our customers. If anything, such legislation would help our prospective competitors. In summary, separate subsidiaries for the Bell operating companies should not be legislated. How to organize most efficiently should be left as a business decision for each company to make.

Thank you.

[The statement follows:]

STATEMENT OF ORMAND J. WADE, PRESIDENT OF ILLINOIS BELL TELEPHONE CO., ON BEHALF OF AMERITECH

My name is Ormand J. Wade. I am President of the Illinois Bell Telephone Company. I appreciate the opportunity to comment on the proposed "universal service" legislation.[1]

Illinois Bell is one of the five soon-to-be-divested telephone companies in the midwest which will become a part of the Regional Holding Company known as Ameritech (American Information Technologies Corp.). The other members of the Ameritech family will be Indiana Bell Telephone Company, Michigan Bell Telephone Company, The Ohio Bell Telephone Company and Wisconsin Telephone Company.

INTRODUCTION AND SUMMARY

In reviewing the bills, we approached each proposal from the perspective and in the spirit that prompted its introduction—achieving a competitive telecommunications marketplace without sacrificing universally affordable basic residential service. Our analysis, however, reveals that adoption of the key provisions would not advance open competition or universal service. Indeed, both objectives would be compromised to the ultimate detriment of the residential ratepayer.

The universal service objective.—A principal feature common to most of the bills is to: (a) ban fixed end-user charges to recover "interstate" non-traffic sensitive subscriber line costs and (b) establish a "universal service fund" to subsidize basic telephone service in so-called "high cost" and rural areas. The combination, as proposed, would not achieve the universal service goal. To illustrate: the urban poor in major Northern and Eastern cities would receive little benefit, while vacation homeowners in Florida and ranchers in the Southwest would enjoy highly subsidized telephone service.

This result is indicative of the problems underlying the universal servide fund provisions. The provisions begin on a false premise—affordable basic telephone service is in immediate jeopardy. They reflect an erroneous assumption that recent FCC decisions fail to assure continued availability of universally affordable basic service.

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[1] The Senate bills include S. 1660, S. 1382, S. 1626, and S. 1667. The House bills include H.R. 3621, H.R. 3440, H.R. 3602, H.R. 3522, H.R. 3366, H.R. 3365, and H.R. 3364.

Finally, the proposed solutions stray wide of the objective. The proposed subsidies would not be targeted to assist those who, if required to pay the full cost, could not afford basic telephone service. Most of the proposed bills—like existing mechanisms—would perpetuate unnecessarily large subsidy pools and, then, spread most of the subsidy revenue to those who can afford to pay the cost of their telephone service.

What may be needed—and what can be developed and implemented—is a more targeted subsidy mechanism. Unlike existing subsidy procedures, more targeted relief could advance the goal of universal service without unduly compromising the goal of a competitive marketplace. The need today is for further research to explore ways to provide necessary subsidies while minimizing the adverse effects on innovation and competition. Enough time exists to perform that research. The FCC's transition plan for access charges, particularly with the modification made on reconsideration, will continue the flow of billions of dollars in subsidies for at least the next several years.

The phased introduction of fixed end-user charges will provide time to evaluate whether, in fact, a universal service problem actually exists. It will provide time to explore and implement sound solutions. In contrast, a legislatively mandated universal service fund at this juncture is, at best, premature and, at worst, would codify a solution which is counterproductive.

The competitive marketplace objective.—As most of the bills recognize, bypass is a reality which must be taken into account. Unfortunately and possibly inevitably, the proposed solutions—"availability" charges and "surcharge" schemes—would stifle competition and innovation.

The proposed charges on bypassers would put the FCC in the untenable position of being a giant handicapper in the competitive marketplace. Moreover, surcharges and availability charges would invite evasion, or development of services designed to minimize subsidy payments, and not to minimize economic costs and maximize efficiencies.

These provisions, as do others in several bills, conflict with the policy of full and fair competition. That policy, which Ameritech endorses for all markets, precludes imposing by regulation or legislation *any* artificial handicaps on *any* competitors. The same rules must apply evenhandedly to all competitors.

Presumably, the objective underlying the surcharges and availability charges is to mitigate existing artificial incentives which promote uneconomic bypass. The intent is sound, even though the solution is not. What is puzzling, however, is that several bills also contain provisions which inconsistently propose handicaps on the divested Bell Operating Companies (BOCs) to the significant advantage of their competitors.

The most troublesome handicap is the proposal which would require each divested BOC to market customer premises telephone equipment (CPE) through a fully separated subsidiary, while no parallel requirement is imposed on the BOC's prospective competitors such as ITT, GTE, Northern Telecomm, IBM and Rolm. Those competitors—unlike a BOC at divestiture—will have a CPE-customer base. Those competitors—unlike a BOC at divestiture—will also have nationwide marketing capability in a nationwide market.

Judge Greene categorically rejected arguments that he impose a separate subsidiary requirement on the divested BOCs. He found that inhibiting the BOCs' provision of CPE would benefit only the BOCs' competitors, to the detriment of the public. For the same reason, legislation proposing a separate subsidiary requirement should be rejected.

Another legislative proposal—the "provider of last resort" provisions—is also inconsistent with full and fair competition. But, more important, such a requirement is unnecessary. CPE and associated wiring—the items the legislative proposals cover—are widely available, even in rural areas. Moreover the FCC Rules already authorize state public service commissions to compel the local franchised telephone company to provide CPE and wiring where competitive alternatives are not reasonably available.

THE FCC'S ACCESS CHARGE PLAN PROVIDES AT THIS TIME THE BEST BALANCE BETWEEN THE TWIN GOALS OF UNIVERSAL SERVICE AND A COMPETITIVE MARKETPLACE

The legislative proposals would ban fixed rate end-user charges for recovery of "interstate" non-traffic sensitive access costs. The motivating factor for that ban appears to be the assumption that the FCC's Access Charge Plan, which calls for phasing in fixed rate end-user charges over 6 years, puts affordable basic telephone service in instant jeopardy. That is not the case.

While the proposed legislative solution is unnecessary from the universal service perspective, it would be highly undesirable from the full-and-fair competition perspective. The FCC's Access Charge Plan fares better only by comparison. To understand why requires evaluation of:

The FCC's Access Charge Plan. The Commission's objective is the same as the goal underlying proposed universal service legislation—a competitive marketplace while retaining universally affordable basic telephone services.

2. Governing economic principles. The objective of competition is to align rates with costs and, thereby, promote efficiency and innovation. The stroke of the legislative pen cannot negate this competitive force.

3. Existing subsidy mechanisms. Relatively few pay the subsidy, while many receive the benefits.

4. Bypass alternatives. Many exist because, under existing access cost recovery mechanisms, bypass alternatives can be priced below the rates charged high volume users, even though the local telephone company's costs are less than the bypasser's costs.

A fair evaluation shows that, given the realities, the Commission has adopted plans and procedures which, if anything, err on the side of attempting to assure universally affordable basic telephone service.

The FCC's access charge order

The FCC, in its Access Charge Order, adopted rules governing both the structure and computation of interstate and foreign access charges; that is, the charges that interexchange carriers and end users will pay to local telephone companies for the origination and termination of interstate and foreign service offerings.

Concluding that a "perfect" access charge plan is unattainable at this time (¶ 121), the Commission adopted access charge rules which, it believed, achieve the "best" balance of its four access charge goals (¶¶ 26, 88, 364). Those goals are:

Universal Service (¶¶ 26, 72, 80–84, 363): The "universal service objective" is to "avoid[] actions that would cause a significant number of local exchange service subscribers to cancel that service." (¶ 80, also ¶ 4). Based on various studies, the FCC concluded that its Access Charge Plan would not cause a significant number of subscribers to terminate their local exchange service (¶ 134 and Appenix G).

Network Efficiency (¶¶ 26, 77, 124, 363) and *Non-discriminatory Rates* (¶¶ 26, 79, 363): In the long-run, only cost-based rates will lead to efficient utilization of telecommunications resources (¶¶ 28–29). Failure to achieve that goal will have adverse repercussions not only nationwide, but also worldwide (¶¶ 112–13).

Prevention of Uneconomic Bypass (¶¶ 26, 78): Bypass is a growing reality (¶¶ 30, 100, 107 and Appendix F). The Commission rejected using its facility-authorization authority to prohibit bypass (¶¶ 30, 110–11, 363). The reality of bypass weighed heavily against continuing to recover nontraffic sensitive access costs on a usage sensitive basis (¶ 107).

To achieve these goals, the Commission's Access Charge Plan initially divides access costs into three major categories, and each of those categories into principal subcategories. The three major categories are (1) non-traffic sensitive exchange access costs, (2) traffic sensitive exchange costs, and (3) special access facilities.

The "controversial" category, and, the one that the universal legislation is directed at, is the non-traffic sensitive category. Initially the Access Plan divides non-traffic sensitive exchange costs into several subcategories.

The dramatic changes occur in the Common Access Line Charge subcategory. Under the Access Charge Plan, as apparently modified on reconsideration, Common Access Line Charges are divided between "*End User* Common Line Charges" and "*Carrier* Common Line Charges." The Plan establishes a formula for determining the portion of non-traffic sensitive costs to be allocated to each category.

The Carrier Common Line Charger element consists of four components:

Premium Access Charge (¶¶ 151–68): Payable by the "AT&T partnership" (¶ 157 n. 57).

Inside Wire Interstate Allocation: Payable by all interexchange carriers on a usage basis (¶¶ 141, 149). This component will phase out with the phase out of the interstate allocation of inside wire costs (¶ 141).

Universal Service Fund: Payments for "high cost" amounts will be made through a Universal Service Fund to be financed by all interexchange carriers on a usage basis (¶ 135). At the direction of the FCC, the Federal-State Joint Board has developed and adopted a formula for establishing the size of the fund and the eligibility rules.

Residual: To the extent that the other three element and fixed end-user charges (see below) do not cover interstate non-traffic sensitive subscriber line costs the FCC provides for a residual rate element (¶ 145). That residual element will be paid on a per-minute-of-use basis by all interexchange carriers (¶¶ 147, 149).

With respect to the End User Common Line Element (*i.e.,* a customer access line charge), the significant feature is the fixed monthly rate which, in 1984, will be $2 per residential line and $6 per business line. The residential rate will increase only $1 per year through 1986.

The FCC's plan also provides a "life line" option within the End User category (¶¶ 136–37).

In 1984, carrier access charges under the FCC Plan will total more than $6 billion. That is, more than $6 billion will be available to hold down basic residential telephone rates.

End user access charges are fair and equitable

The non-traffic sensitive subscriber line between a customer's premises and the telephone company central office is dedicated to an individual customer. That cost is "fixed." That is, subscriber line costs do not vary with usage no matter how many or how few calls a subscriber makes, and no matter what types of calls (local or toll) are made.

The Universal Service Bills, if enacted, would preclude recovery of any "interstate" non-traffic sensitive costs from end users. That ban, in essence, says that it is unfair and inequitable *as a general proposition* for each telephone subscriber to pay the costs that he imposes on the local telephone company. Congress certainly cannot subscribe to that proposition, particularly given the realities of competition and bypass.

As a general matter, each subscriber should pay the full cost of his service. That is sound economics; sound public policy; and, required by the competitive marketplace. To the extent cost-based pricing genuinely compromises the universal service objective for particular individuals, target subsidies might be "fair" and "equitable."

Little debate exists as to the economically efficient and correct answer for recovering non-traffic sensitive (NTS) subscriber line costs. Each subscriber should pay a fixed rate based on the total cost of the NTS subscriber line over which he makes and receives local and toll calls.

As Professor Kahn points out: "customers impose access costs on the system when they are connected to it, regardless of whether they then proceed to place or to receive calls." [2]

Given that fact, non-traffic sensitive costs "should be recovered in a lump sum charge, or, what comes to the same thing, a fixed monthly charge." [3]

Similarly, the Department of Commerce's National Telecommunications and Information Administration (NTIA) has concluded that each telephone subscriber, not the interexchange and exchange carriers, is economically responsible for the total cost of the access line dedicated to his service:

"NTS costs are caused by providing dedicated connections from individual subscriber locations to a telephone central office, . . . i.e., . . . the opportunity to access a particular network or group of networks, not by actual origination or termination of traffic." [4]

Therefore, NTIA concluded, each telephone subscriber, not toll users, should pay for his access:

"There is no cost-causative factor which justifies requiring a heavy user of interexchange services to bear a significant part of the cost of NTS plant that is dedicated to other local subscribers who happen to be light users of interexchange services." [5]

Even those who endorse some form of subsidy to assure universal service acknowledge that:

"Because costs of the subscriber line required for access to the network do not vary with use, the economically efficient solution (in the absence of network externalities) is to have each subscriber pay a flat charge for the line." [6]

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[2] Kahn, "Some Thoughts on Telephone Access Pricing," based on comments delivered at "Workshop on Local Access: Strategies for Public Policy," Sept. 14–17, 1982, St. Louis, Mo., and published by National Economic Research Associates, Inc., p. 3. (Kahn).

[3] Kahn, *Proper Objectives in Telephone Rate Structuring,* 97 Public Util. Fort. 20, 21 (April 8, 1976).

[4] CC Docket No. 80-286, *Reply Comments of NTIA to the Federal-State Joint Board,* Sept. 16, 198[illegible], p. 3 n.1.

[5] *Id.*

[6] "Competition and Cross-Subsidization in the Telephone Industry" (Rand Corp. December 1982), p. ix (Rand Study).

In short, non-traffic sensitive access costs are not "access costs of interexchange carriers," but are costs of the telephone subscribers. Telephone subscribers are the cost causers of non-traffic sensitive access line costs.

The interstate subsidy is a reality

Under existing and contemplated Federal-State developed jurisdictional separations (cost allocation) procedures, a portion of the non-traffic sensitive cost of every subscriber line is allocated to interstate revenue requirements. Recovery of those costs is on a per minute of toll usage basis: the more toll use generated by a customer, the greater the amount of non-traffic sensitive costs he defrays.

As a result, under exising usage recovery mechanisms, each high volume MTS and WATS user pays many times over the total cost of his subscriber line. These excess payments by high volume toll users defray a portion of the access line costs of subscribers who make no or relatively few toll calls; that is, those subscribers who make insufficient toll calls to cover the portion of the access line costs that they cause the telephone company to incur, but are recovered today in toll usage charges.

Relatively few subscribers—business and residence—have sufficient toll volumes to cover fully the portion of the cost of their access line allocated to toll. In 1981, about 1 percent of the nation's business telephone customer locations accounted for approximately 40 percent of business interstate MTS revenues. About 20 percent of the nation's business customers and 30 percent of the residential customers, taken together, defrayed more than 80 percent of the $7 billion in non-traffic sensitive subscriber plant costs allocated to interstate.[7]

The result is that, today, most subscribers pay total telephone charges which fail to cover the total fixed monthly costs incurred by the telephone company in providing them a subscriber line.

The shortage is made up by high volume toll users. That is, the relatively few high volume toll users "subsidize" the vast majority of residential subscribers and many business subscribers. This is not just my opinion. The Rand Corporation, for example, in its December 1982 analysis of "Competition and Cross-Subsidization in the Telephone Industry," concluded after reviewing available data that:

"Substantial cross-subsidization occurs under current arrangements for covering subscriber line or non-traffic sensitive costs. Those who make few or no interstate calls generally pay monthly rates below their subscriber line costs. Many residential subscribers are in this category . . . . These users are subsidized by those who rely heavily on interstate service."[8]

As the Rand Study suggests, the competitive problem is not the "subsidy" per se. Rather, the problem is that the high volume toll users who presently pay the subsidy now have alternatives available which allow them to "bypass" that subsidy:

"With existing cross-subsidies, the concentrated business use of interstate service enhances the attractiveness of bypassing the local network . . . . Even if only a small percentage of business users took advantage of bypass technologies, the reduction in interstate contributions could force substantial increases in rates for intrastate services."[9]

In addition to inviting bypass, two other adverse consequences flow from usage recovery of those customer-imposed access costs, according to Kahn. First, because "the basic monthly service charge is far too low", customers are encouraged to oversubscribe to local service. Second, "the charges for using the long distance network are artificially inflated (on the order of 60 percent)." The proof of the latter consequence is that toll users "contribute to costs that would not be avoided if that usage were curtailed."[10]

Existing and proposed subsidies are not targeted to those who, absent assistance, could not afford basic service

The notion that basic service should be "subsidized" generally is of recent origin. Prior to 1943, no NTS subscriber line costs were borne by interstate toll users.[11]

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[7] A customer who originates, for example, 1000 minutes of interstate MTS use per month (about 45 minutes per business day) pays approximately $140 per month in interstate non-traffic sensitive subscriber plant costs.

[8] Rand, p. 46.

[9] Rand Study, p. 47.

[10] Kahn, p. 3.

[11] Although the 1930 *Smith* v. *Illinois Bell Tel. Co.* decision, 282 U.S. 133 required interstate toll services to bear a portion of common use local facilities, it was a commonly held view in the late 1930's that § 221(b) of the Communications Act overturned that requirement.

The original allocation of NTS subscriber line costs to interstate revenue requirements was designed to permit all subscribers to "share" savings occasioned by technological advances applicable to interexchange services. That same motivation promoted jurisdictional separations revisions in the 1950's and 1960's.

No effort was made to assure that low income individuals benefited from those reductions in intrastate revenue requirements. The reason was obvious: those separations shifts, each of which occurred in the era prior to competition, were not viewed as necessary subsidies.

This is not to say that the need for subsidies was not recognized. State commissions and Congress both acted to provide assistance. For example, Congress provided targeted relief by authorizing the Rural Electrification Administration to make low interest loans to rural telephone companies. As a result, prior to the "separation subsidies," telephone service was available in rural and "high cost" areas.

The failure to target separations and "high cost" funds is the major shortcoming of existing procedures, the FCC's universal service fund plan, and the proposed legislative universal service funds. For example, the high cost payment contemplated by both the FCC plan and S. 1660, would require customers in the depressed areas of the Great Lakes region to provide multi-million dollar subsidies to the fast growing Sunbelt areas:

[In Million of dollars (1984 estimated)]

	FCC Plan			S. 1660 Plan		
	Carrier charges applied to local subscribers	Benefit to local subscribers	Net outflow annually	Carrier charges applied to local subscribers	Benefit to local subscribers	Net outflow annually
Indiana	48.1	23.1	25.0	105.1	81.2	23.9
Illinois	158.5	105.5	53.0	346.1	268.1	78.0
Michigan	114.2	41.9	72.3	249.3	166.2	83.1
Ohio	101.6	56.9	44.7	221.9	171.6	50.3
Wisconsin	43.1	23.5	19.6	94.2	77.2	17.0
Total	465.5	250.5	214.6	1016.6	764.3	252.3

The FCC's plan, despite its shortcomings, is preferable in comparison for two reasons. First, the size of the subsidies is slightly less burdensome—a very important consideration in view of the bypass pressures facing each of the Ameritech companies.

Second, to codify an untargeted subsidy plan—particularly at a time when alternatives are being explored which would better align subsidies with need—would be not only a step backward, but a permanent step backward.

The proposed universal service legislation would continue a subsidy pool which is unnecessarily large to assure universal service; and, therefore, would create unwarranted competitive handicaps and inefficiencies. If Congress is to legislate a subsidy plan, it is essential that the plan: (a) target the subsidies to those who, if required to pay the full cost of their service, could not afford basic service and (b) generate a subsidy pool no larger than essential to achieve the first objective. The proposed legislation fails to move toward either objective.

Bypass is a reality

In its Access Charge Order, the FCC identified numerous instances where bypass is already occurring to the financial detriment of local telephone companies. The FCC identified several technologies which are being used or are being considered for use to bypass the local telephone network: coaxial cable lightguide, microwave radio, satellite, cellular radio, Digital Termination Service, as well as ordinary copper pairs in ducts leased from the telephone company.

Since the release of the Access Charge Order,[12] numerous new bypass projects have been announced. A recently completed survey by Computerworld, which was summarized in a recent article headlined "Large Users to Bypass Phone Companies," shows that the FCC and the telephone companies may have underestimated the bypass threat:

> "Major customers of the nation's telephone operating companies may be migrating to 'bypass' suppliers faster than most industry pundits and government policymakers have predicted. . . . All but one of the seven users contacted—Xerox Corp., Bank of America, General Electric Co., Monsanto Co., MIT, the City of New York and Aeronautical Radio, Inc. . . . are *actively involved in planning or building communications facilities that would bypass telephone company local-exchange networks.* Each organization spends at least $50 million annually on domestic communications, and some spend more than twice that much." [13]

Currently pending before the FCC and in the Congress are proposals by the large cable companies to provide a myriad of local two-way communications sources free of state and, preferably, federal regulation. The cable companies, in their FCC pleadings, freely acknowledge that they are contracting to provide local distribution facilities to MCI and other interexchange carriers. In April 1983, AT&T filed an application with the FCC for a high-capacity satellite transmission service which will permit its customers to have an earth station "located on their own premises." [14]

When bypass occurs, the bypasser avoids paying the interstate subsidy built into message toll rates. Ultimately, the remaining costs will have to be borne by the local telephone subscriber.

The FCC's access charge plan and recent decisions pose no immediate threat to universal service

In its Access Charge Order, the FCC stated that "the continued assurance of universal service" is a major goal, and that "it would be unacceptable . . . to put [an access charge] plan into effect that ameliorates existing efficiency, by-pass and discrimination problems, but which at the same time, had serious consequences for universal service. (¶ 122). The FCC's actions have proven consistent with its words:

1. The Commission has prescribed a gradual 6-year transition to full recovery of non-traffic sensitive subscriber line costs in end user access charges.
2. The Commission is in the process of developing and implementing mechanisms to monitor and quickly spot any erosion of universal service occasioned by its access charge plan or other recent decisions.[15]
3. To assure State participation, the FCC charged the Federal-State Joint Board with the responsibility for determining the size of a Universal Service Fund and the eligibility to draw from that Fund. That Joint Board, which has a majority of state commissioners, has adopted a universal services plan.

Finally, the FCC made provision for targeted life line service exceptions to its minimum end user charges (¶ 136-37). Moreover, the Commission did not foreclose states from adopting innovative state tariff structures which ameliorate any unacceptable impacts that end user charges may occasion.

A recent Rand-sponsored study—a study which supports targeted subsidies—concluded that the move toward end user access charges "would not jeopardize universal service." [16] That study did not take into account the various safety mechanisms adopted by the FCC.

The bottom line is: legislation blocking end user interstate access charges and creating a multi-billion dollar universal service fund is, at this time, ill advised.

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[12] The parties' comments in the Access Charge proceeding reveal that most commentors—even those favoring a totally usage based recovery access plan—acknowledged the reality of bypass:

Consumer Organization Group: "'Bypass' . . . now appears(s) to threaten the viability of the nationwide wire based network." Consumer Organization Group, Aug. 6, 1982 Comments, pp. 6-7.

Pennsylvania Public Utilities Commission: Bypass is a "major threat" which "must be carefully considered in developing the network Access Charge policy." Pa. PUC Aug. 6, 1972 Comments, p. 2.

Florida Public Service Commission: Bypass is a present reality with significant growth potential unless access charges are set at or below the opportunity cost of alternative facilities. Fla. PSC Aug. 6, 1982 Comments, pp. 8-10.

[13] Hirsch, "Large Users To Bypass Phone Companies," Computerworld, Vol. XVII, No. 12, March 21, 1983, p. 1.

[14] *See* "Telecommunications Reports," Vol. 49, No. 17 (May 2, 1983), p. 45.

[15] *See* MTS and WATS Market Structure, CC Docket 78-72 Phase III.

[16] Rand, p. 55.

We do not know enough about the future to assess fully or accurately the problems let alone provide permanent solutions today. Further study and research is needed. The phased introduction of the FCC Access Charge Plan—which in the early years retains billions of dollars of subsidies flowing to local ratepayers—provides the necessary time to assess the situation carefully with further research.

The phased introduction will permit a knowledgeable determination whether, in fact, a problem actually exists. It will provide time to implement any necessary new solutions.

PROVIDER OF LAST RESORT

Several bills would authorize each state public service commission to require local telephone companies operating within its jurisdiction to provide and maintain, upon subscriber request, basic telephone instruments and associated inside wiring. The only restriction would be that the rates for such services would have to cover all relevant costs.

The provisions are unnecessary to assure that all subscribers have available the necessary telephones and wiring. Innumerable general purpose and specialty retailers, such as Radio Shack, as well as mail order firms, sell CPE. American Bell, AT&T's fully separated subsidiary, is marketing CPE nationwide. Distribution channels include (a) national retailers such as Sears, Roebuck & Co., (b) Phone Center stores, and (c) 800-number telephone order desks, with delivery by carrier or U.S. mail to any place in the country. No customer in any part of the country will be far from a retail CPE outlet—and, if a customer cannot or does not want to leave home, he can order by mail or telephone. The existing availability of many channels—national, regional and local; wholesale and retail; store, telephone and mail—makes wide coverage at affordable prices feasible. At compensatory prices, vendors can be expected to offer equipment voluntarily. Therefore, the provider of last resort proposal would not increase the availability of CPE.

Under *Computer II,* telephone companies are free to decide to offer untariffed CPE or not to offer it. If a company were to serve "last resort" customers under state compulsion, but not offer CPE to others, the costs of its "last resort" operations would be very high. These high costs would be reflected in high prices, making the offer to provide "last resort" equipment illusory.

The divested Bell associated companies possibly face an additional problem. If the Commission refuses to lift the structural separation requirement from the divested Bell Operating Companies, some of those companies may choose not to offer CPE generally. If that occurs, the Company might be compelled to establish a subsidiary solely to provide "last resort" CPE—an extremely costly undertaking.

Finally, the proposal singles out one supplier in a competitive market and imposes on that supplier special and, probably, costly burdens. That imposition cannot be squared with the objective of full and fair competition. It runs directly counter to the goal of deregulating competitive markets.

FULLY SEPARATED SUBSIDIARY TO MARKET CUSTOMER PREMISES TELEPHONE EQUIPMENT

The provider of last resort issue dealt with *requiring* a telephone company to provide telephone equipment to a customer. The various separate subsidiary proposals would make it more *difficult* for a telephone company to provide telephone equipment to its customers.

Neither S. 1660 nor H.R. 3621 propose that a separate subsidiary be required in order for a Bell Operating Company to provide telephone equipment to its customers. However, several of the bills propose to do just that. Those proposals are unnecessary and undesirable.

In considering potential revisions to the Modification of Final Judgment, Judge Greene refused to make the divested BOCs' provision of CPE contingent upon establishing a fully separated corporate subsidiary. Judge Greene concluded that, "Based upon a realistic assessment, marketing of CPE presents little potential for anticompetitive behavior by the Operating Companies." [17]

For parallel reasons, the FCC currently is reconsidering whether its existing separate subsidiary requirements covering provision of CPE, enhanced services, and cellular services should apply to the divested BOCs.[18] The Record in that proceeding details the reasons why a separate subsidiary, first, is unnecessary and, second, is unsound policy.

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[17] *United States* v. *AT&T,* 552 F. Supp. 131, 191 (D.D.C. 1982).

[18] Policy and Rules concerning the furnishing of customer premises equipment, enhanced services and cellular communications services by the Bell Operating Companies, CC Docket No. 83-115.

Briefly, requiring a separate subsidiary is justifiable *only* if a company has both the ability and the incentive to engage in anti-competitive activity. With respect to CPE, divested Bell Operating Companies lack both.

The BOCs lack any market power in CPE. At divestiture, each BOC starts with a zero CPE base and in a limited geographic area. The BOCs will immediately encounter in the competitive marketplace AT&T's subsidiary and other CPE vendors, many of whom market CPE on a nationwide basis and have a substantial customer base. Those competitors include ITT, Rolm, Northern Telecom, Nippon, IBM, GTE and many others.

A separate subsidiary requirement would protect those competitors, not telephone subscribers.

The record in the FCC proceeding contains the proof that the BOCs lack any realistic ability to engage in anticompetitive activity in marketing CPE. The record shows that:

(a) local exchange service is not a realistic source to fund predatory prices in CPE or any other market. Based on a similar record, Judge Greene discussed the "several reasons" that the "possibility of successful subsidization of CPE prices with local exchange revenues appears remote." [19]

(b) attempting to fund CPE from other services—such as access charges—will encourage bypass and, thus, the source will evaporate.

The record also shows that the BOCs lack the incentive to engage in predatory pricing of CPE. As the FCC pointed out to the Antitrust Court:

"Predatory pricing in unregulated markets is probably a relatively rare phenomenon because a firm that employs such a strategy would have to forego shortrun profits in the hope that it will be able to realize monopoly profits after competitors have been eliminated. A rational businessman would not adopt such a strategy unless he had reason to believe that predation would be successful. The prospects of success are, of course, related to the relative assets and market shares of the firms in the market. A BOC is not going to start a CPE price war with AT&T because it could not realistically expect to eliminate AT&T (and other firms) as competitors and thus earn monopoly profits." [20]

Judge Greene agreed, stating that although the Bell Operating Companies would have a "theoretical ability to engage in . . . anticompetitive activities" in marketing CPE, "their incentives to do so would be minimal." [21]

The issue, though, is not just the absence of any need to impose a separate subsidiary requirement. A fundamental, affirmative reason exists *not* to impose a separate subsidiary requirement on just the Bell Operating Companies. Such a requirement would be anti-competitive.

Structural separation of the type contemplated in the legislation would impose a significant cost on each BOC deciding to enter the CPE market. That cost would materially handicap the BOCs' competitively, as no other competitor would be required to incur those costs.

Again, the only beneficiaries of a separate subsidiary requirement would be the BOCs' competitors. Certainly, telephone subscribers would not benefit; and, in fact, as Judge Greene made clear, not allowing the BOCs to compete fully in the CPE market would be contrary to the public interest.

Mr. **Hayes**. Mr. Chairman, members of the committees: I am John Hayes. I am vice president—revenues and public affairs for Southwestern Bell.

Changes taking place in the telephone industry are generating many questions concerning universal service, increasing telephone rates, depreciation procedures, and the implications of bypass. I would like to take the time allotted to me to speak specifically about the nature, extent and implications of bypass. As you have probably surmised by now, it is of concern to all of us.

Incidentally, yesterday's FCC decision will not be out in final written form for about 2 weeks, but from what I know of it, it would not have caused me to change my remarks, other than to say in regard to bypass, it appears to further exacerbate the problem.

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[19] 552 F. Supp. at 192.

[20] *See United States* v. *Western Electric Co.*, C.A. No. 82-0192 (D.D.C.), Brief of F.C.C. as *Amicus Curiae* (April 20, 1982).

[21] 552 F. Supp. at 191.

Bypass, as you know, is generally understood to mean the origination and/or termination of a call without the use of a local telephone company's plant. Bypass results in a loss of revenues to the local telephone company. It is no more than another word for competition.

To establish an historical perspective, there were, it seems to me, two fundamental factors which led to the development of bypass. One was the social policy of having long distance service subsidize local service to help meet the Nation's universal service goal. While this pricing policy did indeed help us achieve universal service, it most certainly placed an uneconomic cost burden on heavy users of long distance.

The other primary factor relating to bypass was technology. The technological changes which have occurred and are occurring in the industry significantly lowered the cost of entry into the business. As a result, technology provided the wherewithal and the toll subsidy provided the incentive for bypass.

Who are the most logical users of bypass technology? Bypass appears to be a current option primarily for large business customers responsible for significant amounts of long distance traffic, and this group represents an extremely high risk for Southwestern Bell.

As you are aware, a telephone company's business revenues are concentrated among a very limited number of large business customers. In addition, these large customers are generally clustered in very tight geographical areas. For example, Southwestern Bell has just over 1,250 switching centers or wire centers. Five, only five of these wire centers, just four-tenths of 1 percent, account for 10 percent of our entire business message toll service revenues. And a mere 10 percent of our wire centers account for two-thirds of our total business MTS revenue.

This point on geographic concentration merits emphasis. It means that a bypasser need only build a system to handle high-volume traffic originating from a small geographical area. They need not replicate the entire ubiquitous plant. Bypass systems built to serve a specific geographical area also allow small and medium-sized businesses, who could not afford to build their own facilities, to cost-effectively bypass us by hooking up to the bypass company's facilities.

Bypass is not reserved for toll business alone. It can also be used to circumvent local exchange service. There are any number of examples I could recite, but the message would not change. Bypass is here now and will continue.

As for the potential consequences, as bypass grows the following scenario will unfold. As large business customers deploy their own bypass systems and leave the local network, fewer customers remain to share an increasingly larger portion of the company's plant investment. Thus, remaining customers will primarily be comprised of residential and small and medium-sized business customers.

Rates must rise to recover the cost of that investment, and as rates rise more customers find it economically beneficial to leave the network in favor of bypass technology. As a result, the telephone company is left serving the high-cost, low-revenue customers. Or, in a strict economic sense, we end up losing the winners and winning the losers.

If access charges are established at too high a level, carriers and large customers will flee the network in favor of bypass systems, thus stranding telephone company investment, and low-volume users may be forced off the network, stranding investment and leaving us with a serious social and political dilemma.

I want to assure you that displacing local customers is not more palatable to us than it is to you. In addition, we must address the need for improved capital recovery methods and schedules appropriate to a competitive environment instead of a monopoly environment. To effectively compete, we must move to a more realistic capital recovery ratio.

If the local network is not upgraded to meet the needs for new services, like digital traffic at high data speeds, then either the customer or the inter-exchange carriers will initiate some form of bypass. And as technologies are developed which lead to economic bypass of the network, it is critical that we have the ability to deploy similar technology in order to remain competitive.

In closing, Mr. Chairman, let me offer for the joint committees' reference a comprehensive study of network bypass, done for us over the past several months by Touche, Ross & Co. in conjunction with our own people. We developed this plan to help us understand and more effectively deal with bypass from a technological, marketing, and regulatory standpoint. Copies are available to the committee.

Thank you.

[The statement follows:]

STATEMENT OF JOHN E. HAYES, VICE PRESIDENT—REVENUES AND PUBLIC AFFAIRS, SOUTHWESTERN BELL TELEPHONE CO.

Mr. Chairman, members of the Committees, my name is John Hayes. I am Vice President-Revenues and Public Affairs for Southwestern Bell Telephone Company.

I'd like to thank the Senate Commerce, Science and Transportation Committee and the House Energy and Commerce Committee for the opportunity to appear today and represent the views of Southwestern Bell.

The subjects outlined for discussion today, including that of the bypass of the local telephone exchange network which I will address, are in combination the fundamental elements of national policy direction which will guide our future.

Those of us representing Bell Operating Companies here today share a common history, operating as parts of a national system, guided by a long-standing national policy. Our future holds promise as we embark on courses separate from each other, however we remain united in our individual commitment to serve the American public. .

I have included in this testimony Southwestern Bell Telephone Company's views on several issues which are the subject of current legislative proposals. The issues of universal service, access charges and bypass are inexorably intertwined.

UNIVERSAL SERVICE

This concept, expressed in the 1934 Communications Act as a national goal, though not precisely defined, was broadly understood to mean the nationwide availability of telephone service. Technology was such that there was no need to define what "telephone service" meant. The functional method which was adopted as the means to achieve that goal required the companies to operate as utilities in a monopoly environment under government regulation. It required the companies to deliver "service" to all persons requesting it within state franchised territories.

Clearly the technological explosion in our industry over the last several years and the sense among our federal regulators that the universal service goal had been realized combined to motive the introduction of competition into what was a regulated monopoly environment.

While the 1934 Act remains the law of the land, and still includes its historical national goal, the several bills about to be considered seek to maintain the universal service goal. We believe that the functional method of realizing the universal service goal has been unalterably changed. And, that this demands a commensurate new understanding of the national policy objective for the future. None of the bills presently introduced defines the meaning of "universal service." We believe it is essential for any new amendment to the 1934 Act to define that term. In this way, public expectation, regulatory behavior and corporate initiative can be channeled in a common direction and contribute to a common good. We suggest that that term means the provision of access to the two-way switched voice telecommunications network. The access itself should take the form of a wide range of service options and choices in capability, quality and rates, that are designed to be responsive to our customers' economic and calling needs. Through such alternatives, we would seek to maintain the current levels of telecommunications development.

In our service territory of Arkansas, Kansas, Missouri, Oklahoma and Texas, we serve over 8,500,000 customers. We and our customers live and work in as dynamic and diverse a set of rural and urban environments as may be found in our country. Our concerns for universal service embrace the whole of this diversity.

Certainly there can be no question that competition drives prices to cost. This is a fact reflected in our proposals to reprice basic telephone service offerings in each of our states. It is equally true that competition creates increased consumer choices of products and services. This fact is also reflected in our proposals and is a key to maintaining universal service.

While the details of our rate proposals reflect the significant differences between the conditions in each of the states, we seek in all states to bring a variety of different service offerings to our customers. We propose to offer these options in as great a variety as we can, in as many locations as we can, and let the consumers choose for themselves those service options best suited to their individual social, economic and service needs.

As we go forward, we expect local telecommunications services to remain the core of our regulated business. But, we also expect to pursue new service opportunities, viewing our past as a base to build from, not a shell to remain under.

We look forward to making our local exchange network a workhorse vehicle for delivering new services and new consumer options throughout our territory. Our commitment to that future is no less strong in the rural areas than the urban centers.

As these services are brought to the marketplace, universal service in the context of the term earlier described, is as critical a requirement for our commercial interests as it is a requirement of the public interest.

ACCESS CHARGES

Under existing and traditional arrangements, about 25–30 percent of local exchange distribution (non-traffic sensitive) costs are charged to the interstate jurisdiction and are recovered through rates for interstate long distance usage. The balance of those costs are charged to the intrastate jurisdiction. These are recovered through rates for intrastate services, particularly long distance and optional local services and equipment.

Recognizing that the competitive nature of long distance services dictates that these services must necessarily be priced based in relation to their own costs, the FCC decision in Docket 78–72 calls for a phased-in recovery of non-traffic sensitive local exchange costs from local exchange subscribers. While we recognize this decision is under reconsideration and is subject to change, the plan remains the focus of most legislative proposals.

Under the FCC plan interexchange carriers would pay us and other exchange companies fees to cover costs of providing interconnection to our local network; over time these would be fully traffic or usage sensitive rates. The end users, our subscribers, would be charged a fee for the non-traffic sensitive costs of connection to the network, including connection to the interstate and intrastate long distance network.

This approach would eliminate the assignment of costs to one among several competing long distance carriers. It would allow nondiscriminatory charging of all interconnecting carriers for like services. It would avoid economic incentives for those carriers to bypass our local exchange and build directly to larger and more profitable users. It provides a reasonable certainty of recovering local exchange costs associated with providing customer service.

The major perceived deficiency in the Order is its effect on the local exchange customer who uses little or no long distance in a given billing period. This customer would pay a monthly charge for interstate long distance network access and a charge for intrastate long distance access. These charges would be the same as those billed a customer who does make long distance calls.

In addition, the Order only deals with the bypass issue in terms of interexchange carrier bypass. Existing customer and non-carrier bypass is a part of the issue not addressed by the FCC's plan.

While the FCC's Order provides local exchange carriers with some flexibility in proposing interstate access charge rate levels during the transition period, the Commission's Order leaves no flexibility as to its ultimate objective which is that all interstate NTS costs are to be recovered from customers on a fixed basis rather than from carriers on a usage sensitive basis. Said another way, the flexibility is in the implementation process, not the end result.

Many alternatives to the FCC decision are being considered in current legislative proposals. However, any alternative adopted should provide equity among competitors, create reasonable certainty of cost recovery to local carriers, discourage the bypass of local exchange networks, and provide equity to our customers.

Most of the bills now being considered seek to overrule the FCC decision and spread the costs in question among interexchange carriers. Some of the bills seek to avoid the incentive this would create to bypass us by levying a fee on privately owned systems and others who bypass the local exchange network.

Certainly the FCC's access charge decision was considerate of the negative impact of bypassing of the local network. Legislative and regulatory actions are capable of going beyond avoidance of a threat to universal service. The perspective of the local exchange network as the vehicle for delivery of universally available consumer access to the promise of an information age is attainable by the actions of the Congress, the FCC, and our state utility commissions.

BYPASS

I know that each of you is aware of bypass—or the origination and/or termination of a call without the use of the local telephone company's plant. But the nature, extend and impact of bypass on the local telephone companies is a subject which I believe to be among the most important in the telecommunications industry for the foreseeable future.

The effect of bypass is a loss of revenue from both local subscribers and interexchange carriers. In a bypass configuration, traffic is divereted from the local telephone network. The lost traffic means lost revenue. Furthermore, the remaining subscribers must pay higher rates in order to compensate for the revenue lost through bypass.

When bypass occurs, large users (which are generally businessess) divert substantial traffic from the local plant and route the traffic by another means. The effect on the telephone company's costs would be as follows:

1. Non-traffic sensitive costs (e.g., depreciation) associated with the plant idled because of bypass would not be reduced.
2. Some traffic sensitive costs may eventualy be reduced. However, operating and maintenance costs would take some time to adjust to the reduced traffic on the network.

The loss of revenue without a proportionate reduction in costs would reduce the company's net operating income. A reduction in net operating income can be expected to adversely affect the telephone company's ability to earn its authorized rate of return and its ability to raise capital. After all, once divestiture occurs, the local exchange companies such as Southwestern Bell must compete in the marketplace against one another, AT&T, and other corporations for capital. Erosion of financial performance because of bypass will increase the cost of capital in the marketplace as investors demand larger returns to compensate them for the increased risk of investing in a telephone company experiencing income losses due to bypass.

In addition, all remaining customers (including small business and residential customers) would have to pay higher rates to adjust for the withdrawal of large user traffic from the local network. This would occur because the remaining customers would have to assume the revenue requirement for essentially the same level of telephone company plant and expenses. The effect of concentrating capital recovery charges on a shrinking customer base would encourage additional bypass.

The risk of loss is increased because local telephone company revenues tend to be concentrated disproportionately among a small number of business customers. In addition, revenues tend to be concentrated geographically.

This concentration increases the vulnerability of local telephone companies to bypass since revenues can be disproportionately affected whenever (a) major business customers move to a bypass system and/or (b) bypass technologies are introduced into the small geographic area covered by high revenue wire centers. This last point on geographic concentration deserves emphasis. It means that a competitor to the local telephone company need only build a bypass system to handle high volume traffic originating from a limited number of large customers in a small geographic area. The competitor does not have to replicate the entire ubiquitous local plant.

Bypass can be described as either uneconomic or economic. These can be defined as follows:

Uneconomic bypass.—Occurs when a competitor with higher costs than a local telephone company is able to price its services to customers at a price lower than the local telephone company.

Economy bypass.—Occurs when the price of telephone service is cost-based, but a lower cost provider (probably using a different technology) is available.

Both forms of bypass have a negative effect on a local telephone company's revenues. However, my testimony refers to *uneconomic* bypass.

BYPASS TECHNOLOGY

Several technologies can be used for the purpose of bypassing the local telephone company's plant. In the recent past, especially in the last decade, technological alternatives to the telephone company's copper wire have been developed and marketed to meet local transmission requirements, especially the requirements of large business customers. I have summarized the categories with a brief discussion of the major categories:

1. Private microwave and radio systems

General description.—Radio systems.—Microwave radio (point-to-point) requires line-of-sight between the transmitter and the receiver. Due to frequency congestion in urban areas, the microwave bands below 18 GHz (gigahertz) are practically unavailable for private point-to-point systems. However, capacity exists in the higher bands to implement systems to carry traffic between sites within a Local Access and Transport Area (LATA) without using local telephone company circuits.

Digital Termination Service (DTS) is the foremost application of point-to-multipoint microwave used for bypass. DTS can deliver data from one point to another point within a LATA or serve as a gateway to an interexchange carrier's system. Interexchange carriers with DTS licenses can move high speed data between and within LATA's without use of local telephone company circuits at either end. The initiation of DTS is only one to two years in the future. A number of common carriers have recently been licensed by the FCC to provide DTS sevice in the Southwestern Bell region.

Cellular radio constitutes a new public mobile and portable communications offering by common carriers. In its mature configuration, a nation-wide cellular system can potentially bypass the local telephone company plant while switching calls to destinations which may be mobile or fixed, as well as local or in another LATA. Under FCC policies, each Standard Metropolitan Statistical Area (SMSA) will have two competing cellular radio systems, one of which will be operated by the local telephone company.[1] This means Southwestern Bell will compete with another carrier in several major urban markets in its region.

2. Bypass examples—Radio System

General Electric has recently begun marketing a 23 GHz radio system (GEMLINK). Promotional literature emphasizes that GEMLINK is (a) less expensive, (b) available sooner, and (c) more under customer control than leased telephone company circuits.

Examples from the trade press include the following:

ICOM, a private company whose principal outside shareholder is CIGNA Corp., the parent of two insurance companies (Connecticut General and INA), was authorized by the FCC to construct DTS systems in 18 cities, including San Antonio, St. Louis, Kansas City, and Tulsa. (Satellite News, March 7, 1983)

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[1] The other system will be operated by a "non-wireline carrier" which will be a company other than the local telephone company.

Westinghouse has developed a private radio network to connect 20 sites (15,000 phones) in the Pittsburgh area. (Communications News, May 1981)

Federal Express was authorized by the FCC to construct DTS systems in 14 cities in order to create a high speed facsimile network; Dallas and Houston were among the 14 cities. (Satellite News, March 7, 1983)

IBM has contracted with Motorola to buy portable (one-and-a-half pound) radio terminals for use in a nationwide private digital communications network which will enable field representatives to communicate with headquarters without the use of local telephone company facilities. (Data Channels, March 21, 1983)

GUIDED SYSTEMS [2]

1. General description—Guided systems

Guided systems included coaxial cable and fiber optics. A bidirectional cable television plant can be used to provide bypass transmission facilities for individual subscriber telephones, either business or residential, in areas in which the cable television franchise holder elects to operate such a service.

With the placing of cable where there is geographic concentration of businesses, many services become subject to competition. While the initial placement might be for the purpose of high speed data transmission or other similar services, the connection of that cable to an interexchange carrier would raise the possibility of bypass for data services as well as long distance service.

In addition, with cable television's penetration of U.S. households (currently approximately 25 percent) increasingly using new bidirectional cable systems, cable can be used not only to route calls to an interexchange carrier for transmission out of the LATA, but even to another phone on the same cable system. This is the first bypass technology which we discussed which could someday compete fully for residential and small business telephone traffic. This represents a significant potential future loss of revenue for local telephone companies.

Fiber optics technology has recently developed to the point where it will be rapidly introduced into communications systems throughout the 1980's. One main advantage of fiber optics systems is their ability to carry high speed data transmission. In comparison to the telephone company's copper wire network, fiber optics systems are attractive for local or short distance distribution of concentrated high volume traffic.

2. Bypass examples—Guided systems

Prince George's County (Maryland)'s system is an example of a cable television system which is being expressly designed to provide private switched voice, video, and high speed computer circuits to subscribers in the 720,000 resident county adjacent to Washington, D.C. In fact, most new cable systems in urban markets are being designed with current or future two-way capability.

Satellite transmission systems

As of August 1982, fifty-six receive-transmit earth stations were licensed by the FCC to operate in the five state Southwestern Bell Region. Of these, 17 are classified as "private" and used by the licensees to route long haul traffic without any use of local telephone circuits. In addition, 34 earth stations are licensed to common carriers, some portion of which, I assume, are located on customer premises and are not using local telephone company circuits.

In addition, the following announcements have appeared recently in the trade press:

United Services Automobile Association has formed a subsidiary, USAA Satellite Communications Company, to resell long distance satellite services to businesses in San Antonio, Texas; traffic will be routed through a customer premise earth station at USAA headquarters.

Atlantic Richfield signed a contract for Harris Corporation to design a private satellite network to link corporate facilities in six cities, including Dallas. (Telephony, September 7, 1981)

MCI will buy capacity equivalent to 24,000 circuits in two Hughes Galaxy satellites. MCI will access the satellites through earth stations in major cities, including Dallas. (Satellite News, February 7, 1983)

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[2] Guided systems confine transmission to narrow physical paths (e.g., wire, fiber, or cable) as opposed to "unguided" systems in which energy is received "over the air" (e.g., radio).

United Press International will buy up to 2,000 earth stations with two-foot antennas as part of its project to eliminate use of all terrestrial telephone company circuits—both local and long distance. These small earth stations will be located on the premises of all UPI customers, many of which are located in Southwestern Bell's region. (Satellite News, January 31, 1983)

Atmospheric optical systems

Atmospheric optical systems are not in widespread use at this time. The sole example which we identified was Phillips Petroleum which used an infrared light to provide a data circuit between two buildings 1,500 feet apart in Bartlesville, Oklahoma. (Communications News, May, 1982)

These examples I have cited should be considered illustrative rather than all inclusive. Announcements of bypass systems being implemented occur regularly in the trade press.

The real threat from these alternative technologies is that they will be combined into networks by interexchange carriers acting on their own or as part of joint ventures with local distributors of traffic. The carriers will then offer end-to-end service which can originate and terminate calls without using the local telephone companies at either end. Traffic will be routed around the local public telephone network which will be underutilized and more expensive for its remaining subscribers.

EXTENT AND TYPE OF BYPASS IN THE SOUTHWESTERN BELL REGION

Bypass already occurs among Southwestern Bell's largest customers. Approximately one in four engages in some form of bypass.

Furthermore, in terms of future plans, approximately two out of three either engage in bypass now or expect to do so within the next three years.

In order to estimate the incidence of bypass, Southwestern Bell recently engaged Touche-Ross Company to analyze the extent and type of bypass in the Southwestern Bell region. A sample of telecommunications managers from a universe of 320 of Southwestern Bell's largest private sector customers was surveyed.

This is a high risk group for Southwestern Bell because revenues are disproportionately concentrated in a small number of business customers.[3] Loss of large customers can have a ripple effect through revenue requirements in several categories. Bypass means not only the loss of access charge revenues but also revenues due to such sources as private lines and intra-LATA toll.

Based on the sample, approximately 25 percent of Southwestern Bell's 320 largest revenue producing customers currently use one or more technologies to bypass local telephone company plant. While we are still in the process of determining the adverse revenue impact associated with this bypass activity, the size of these customers and their volumes of business assure that the associated revenue loss is high.

In addition, as mentioned above, two out of three of the respondents either use now or plan to use systems or carriers other than the local telephone company for bypass within the next three years.

An examination of bypass activity shows that it ranges across industries and is not limited to particular industries. Based on total company sales reported by the respondents in the study, there is an identifiable upward trend in the incidence of bypass as the dollar volume of reported sales increases. This provides reinforcement for the concept that the larger the customer, the higher the probability that he will engage in bypass.

The most logical users of bypass technology, the large business customers, are generally clustered in very tight geographical areas. For example, Southwestern Bell has just over 1,250 wire centers. Five of these wire centers—just 4/10 of one percent—account for two-thirds of our total business MTS revenues.[4]

Bypass systems built to serve a specific geographical area also allow small and medium-sized businesses—who could not afford to build their own facilities—to cost effectively bypass us by hooking up to the bypass company facilities.

And bypass is not reserved just for toll business. It can also be used to circumvent local exchange service. Let me share with you a couple of examples existing today in the Dallas-Fort Worth area to show you how bypass can work on both levels.

Texas Plaza, a new office and residential complex near Texas Stadium bills itself as the "first mixed-use office complex in the world linked to a digital satellite communications network."

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[3] For example, as shown on Attachment 1, one percent of business customers account for one-third of business MTS revenues while five percent account for 55 percent of such revenues.

[4] See Attachment 2.

The satellite network will provide a variety of services like video teleconferencing, electronic mail, voice and data communications. And this system is being provided not by Southwestern Bell but by an Atlanta-based company.

Another example may be found at the Los Colinas development were a two-way cable system, along with the purchase of an independent switching machine, has taken a significant number of local telephone customers and main stations right out of the local and long distance telephone network.

There are any number of examples I could recite, but the message remains the same. Bypass is here and it is likely to grow. As for the potential consequences, as bypass grows, the following scenario will unfold.

As large business customers deploy their own bypass systems and leave the local network, fewer customers remain to share an increasingly larger portion of the company's plant investment. Those remaining customers will primarily be comprised of residential and small and medium-sized business customers.

Rates must rise to recover the cost of that investment. As rates rise, more customers find it economically beneficial to leave the network in favor of bypass technology.

As a result, the telephone company is left serving the high cost, low revenue customers. Or, in a strict economic sense, we end up losing the winners and winning the losers.

I believe that the Touche Ross study and the statistics to which I have referred make the financial vulnerability posed by bypass competitors abundantly clear. Because of the very high percentage of revenues produced by a relatively small number of business customers in a few concentrated locations, Southwestern Bell must have the ability to compete equally with any competitor if we are to have a fair chance to maintain a solid financial base for the future. While this discussion has focused primarily on Southwestern Bell's experience with bypass, the impact of bypass is of equal concern in all regional operating companies.

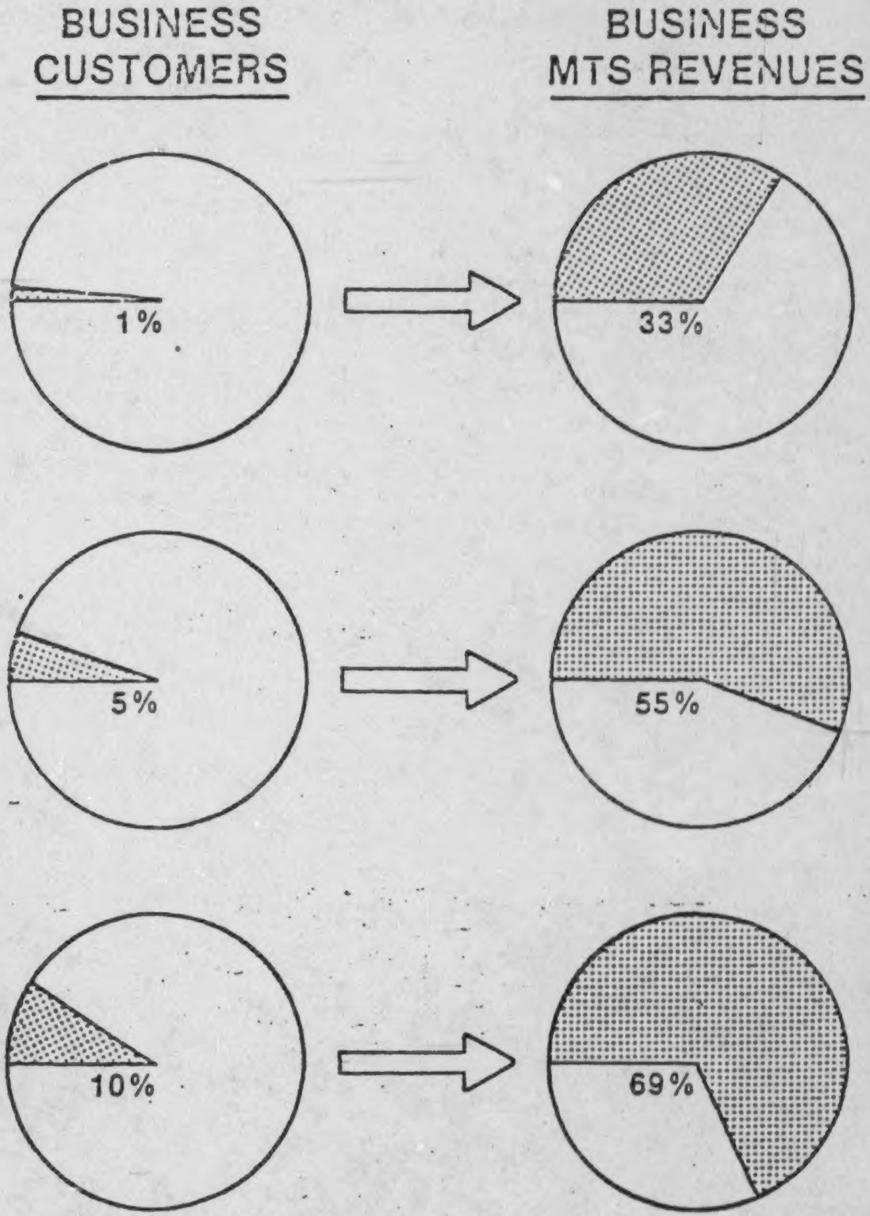
The existing legislation does not, for the most part, provide significant guidance on how the proposed bypass levies would be assessed, by whom they would be billed or to whom they would be remitted, how the distribution of the funds generated would be made and to whom they would be paid. Certainly, any assessment made for bypassing a local exchange company should be returned to that same company. None of the present proposals make that assurance.

It is our hope that we can work with the Committees in charting a course that will assure the promise of the information age is realized for all the people.

Thank you for the opportunity to appear today.

ATTACHMENT - I

SOUTHWESTERN BELL BUSINESS CUSTOMER CONCENTRATIONS

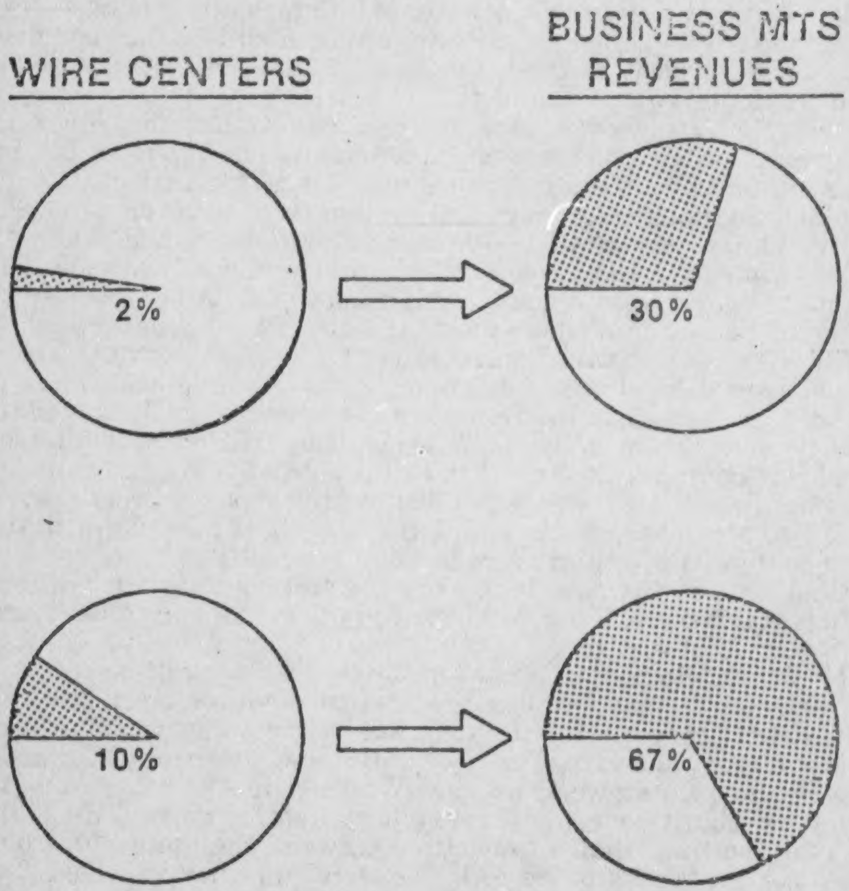


ATTACHMENT - II

SOUTHWESTERN BELL WIRE CENTER CONCENTRATIONS

Southwestern Bell has over 1250 wire centers. 5 of these wire centers (4/10 of 1 percent) account for over 10 percent of Southwestern's business MTS revenues.

ADDITIONALLY:



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Chairman Packwood. Thank you.

Mr. Smith, Andy Smith, let me address this question to you, and if you want someone else to answer it that is fine, although my hunch is there would not be any difference between the companies.

Just to make sure we are all talking about the same thing, would you define what you mean by "bypass"?

Mr. Andrew Smith. Bypass to me is where there is a source of communications ability in existence for whatever the service need might be, whether it be data, voice, video, or the whole range of communications facilities that for one reason or another, either on an economic basis or on an uneconomic basis, if there is a subsidy involved, the customer finds it advantageous to find another path beyond and around our serving facilities to achieve his communications needs.

Chairman Packwood. You mean around the long-distance facilities or around the local facilities?

Mr. Andrew Smith. Either actually is bypass.

Chairman Packwood. When the term bypass is used by you do you normally mean in the sense of their bypassing the total system—interstate, intrastate, intracity—or do you mean they are hooking into your local system some place, but they are bypassing the long lines or long distance?

Mr. Andrew Smith. No. To me, Mr. Chairman, it means simply that they are bypassing some part of our facilities that could provide those services to them for reasons that are advantageous to that particular organization.

Chairman Packwood. Now, to the extent that they hook into your local system, they may bypass your national system, but here I am talking about the long lines and the AT&T part of it. To the extent they hook into your local system, you would have no difficulty in knowing who they are and finding them, would you?

Mr. Andrew Smith. I would think that would be workable. They could, of course, also bypass our intrastate LATA approach, which is the other side that comes out of the divestiture situation.

Mr. Raymond Smith. Senator, may I comment on that? Yes; we would have difficulty. For example, bypass by large customers will be both the long-distance network and the exchange lines, and they will be doing both at the same time. They will connect into some local lines because they want to call people, say, in Philadelphia or Pittsburgh, but they will put a dish on the roof, and that dish will go off to a transponder in a satellite and come back down to some vendor that will connect them to all of their plants.

Chairman Packwood. Wait. You are talking about two different things right there. I am talking about first the ones that connect into your local system.

Mr. Raymond Smith. What I am saying is they will do both.

Chairman Packwood. I understand they will do both, but to the extent that they connect to your local system can you find them?

Mr. Raymond Smith. Well, we will know, for example, that it is Westinghouse, and we know that Westinghouse is a bypasser, OK. We know that they connect into our system for some of their lines, but for the lines that, in effect, go between the main office buildings and the plants in western Pennsylvania, they will have facilities on their own property that do that.

Chairman PACKWOOD. They should have a private wiring system is what it is.

Mr. RAYMOND SMITH. It is a private microwave and wiring system. That is what it is.

Chairman PACKWOOD. Up until the FCC statement yesterday, how did their original access charge system catch those bypassers?

Mr. RAYMOND SMITH. The way it caught it, Senator, was the fact that we were going to apply the costs at the local loop plant where they belong so we could bring our costs down to a level that we could compete on an economic basis with Westinghouse, Reliance Insurance, or anyone else.

Chairman PACKWOOD. That is what I mean. It was not going to catch the bypassers. That is my question.

Mr. RAYMOND SMITH. It was not going to catch the bypassers.

Chairman PACKWOOD. And my question was how did it catch them, and the answer is that it does not catch them. It simply says that we are going to put you on the same footing as them.

Mr. GUINN. Well, it does not even quite do that, I do not think. There are two types of bypass, private bypass and carrier bypass, and carrier bypass is much more onerous because three or four customers can go together, or you can be in a shopping center complex, put a satellite on a roof, distribute in that complex and completely bypass everything.

But what the FCC access charge order does—it is the best plan that has been proposed so far to avoid bypass—is to charge some of the costs as a CALC directly to the end user.

So there is less incentive to bypass. It also sends a clear signal, because it says that over the years the non-traffic-sensitive costs are going to be phased into the end user. It sends a clear signal to the private bypasser, and the public bypasser, that it is going to be less financially advantageous for them to bypass, because downstream these costs are going to be paid by the end user, no matter whether he uses their services or our services, and so the economic incentive for bypass decreases.

However, it still does not protect us completely, because as I said, we have been able to demonstrate that some of our largest customers could bypass us for a penny a minute, which is about one-sixth of what we are going to be charging the carriers for interstate access charges.

Chairman PACKWOOD. Now, to the extent that the FCC yesterday seems to indicate that they can find bypassers and catch bypassers—I will take their word for it—then what is wrong with the system that is proposed by either Congressman Wirth or Chairman Dingell or myself in terms of catching the bypassers—not for the moment arguing the philosophy, but catching the bypassers?

Mr. STALEY. Senator, may I comment on that?

I believe there is some confusion as to what they were exactly speaking to. They were actually talking about services that are message-type services and applying access charges to those services. In other words, those were services that would be ordered from us under tariff, and therefore, we would be in a perfect position, of course, to assess the access charges to those type services.

On the other hand, there are services that completely bypass our network—and there are many that completely bypass. Under the new setup you can put in your own switchboard, you can put in your own local facilities, your own toll facilities and completely bypass the network. And that is exactly what is being done today by many large customers in lower Manhattan.

Chairman PACKWOOD. Let me ask you this, though. Everything that bypasses your system is still licensed by the FCC. Nobody puts up satellites and nobody uses any kind of signals that the FCC does not know about.

Mr. STALEY. That is correct, except, though, that the intent and why they are providing those services we do not have the slightest idea. If it is to improve or put an additional service on their existing facilities, we have no idea what that service is being used for.

Chairman PACKWOOD. All I am saying is that indeed we know they exist, and they are not allowed to transmit without approval of the FCC.

Mr. CLENDENIN. One final point. The technology of bypass is leaping forward almost as fast as all the rest of technology is, and you have to go back to the basic intention that has led to this phenomenon.

The bypass phenomenon is not interested in working on that which is a cost-based price. It is going to work at those prices which it knows are carrying a subsidy—the very things that have been the basis for the preservation of universal service. So you really have a vicious circle here when you start to recognize that if you do too much to burden carriers, you may actually create a higher incentive for bypass; and the balance point that the FCC has been trying to reach has been to push some of that subsidy to the end user, some of the burden to the carriers and create a balanced situation which would not promote an even worse situation. It is a very sensitive problem of balance.

Mr. HAYES. Senator, if I may——

Chairman PACKWOOD. I have used up our time. We are not going to have any votes, but the House Members may, and I want to give them a chance to ask questions.

Mr. Wyden.

Representative WYDEN. I thank the chairman for his graciousness.

Let me start, Mr. Smith, and ask you a question and start by telling you you that your company has been a good corporate citizen in my congressional district. We have recently computerized child care services in Portland. Your company was the first to make a donation to make it possible for working women to get these kind of services through computer, and I congratulate you for it.

I am particularly concerned about the FCC's decisions as they affect the elderly and small business. Those are two constituencies that I think are important in any decision we make. And let me focus on small business for a minute. I am going to go slowly because I think this is the key concept, certainly for this Member.

Now, my concern is that small business in this country with respect to telephone service is going to be hit with a very, very hard one-two punch. By going to a measured service system as you have proposed to do in Oregon, a small business which generally makes a small number of long-distance calls but a large number of local calls is going to be hit with a very large increase in basic phone service. That is punch No. 1.

Punch No. 2, which in effect makes a bad situation worse, is that we have got the FCC's access charge decision, which even at the beginning is going to cost more than half of all the small businesses more each month just for access charges than they generally pay in long-distance charges.

So my question to you is: Don't you think that we are being pretty hard on small business with these telephone changes that are being made? Small business creates most of the jobs in this country. My State is fairly typical. More than 80 percent of the new jobs come from small business, and I just cannot figure out why small business is being singled out through your kind of approach, plus the FCC decision, for such a disproportionate share of the burden, given the fact they are where our economic growth is going to be.

Could I have your response?

Mr. ANDREW SMITH. Certainly, Congressman. I think it may be inappropriate to suggest that small business has been singled out either by us or by the FCC in their actions. Our approach to basic measured service, as I think you know, in the State of Oregon filing is that it is our expectation that the majority of the customers in any given class of service will realize a reduction in this fashion. There are some heavy users of small business—the real estate business that was mentioned by Commissioner Leisner previously—and I think here perhaps we come to a difference of philosophy.

It is my opinion that the user of the service, going toward a competitive environment, that the user of the service that uses it more must pay more for that service usage. And this is a philosophy, of course, that will allow us to keep the rates lower for the elderly, for the poor, if you will, and for the people who find it possible to use their telephone service a bit less driven by economic necessity.

Now, to the extent that there is some need for support—and I realize that is the basic thrust of the two bills that we are fundamentally considering—that should be targeted to those people who need that kind of help. But we will be working with those small businesses, as well as the large businesses and the other customers. We will start—I am not sure what month it is—giving them duplicate billing and working with them in order to help them see whether or not the present service they have serves them best or whether there are other alternatives.

But we believe that with the changes that we are going through at this time that the alternative does not unduly burden that particular aspect of business. At least that is our view at this time.

Representative WYDEN. I think the evidence shows that small business is going to be hit very, very hard by these changes. The last study we have indicates that 62 percent of the businesses in this country made under $7 a month of long-distance calls. Now, the study is a few years old, but we are talking about $6 a month for access charges alone. And I would just hope that you would expand the universe of solutions that you are looking at in our region rather than just focus on this local measured approach for small business.

Do you consult with any of the small businesses?

Mr. **Andrew Smith**. We certainly do, Congressman. And one of the experiences we are realizing right now is a very significant trend of small business customers to measured service. As you know, in our State we have had some fairly significant increases prior to this divestiture consideration, driven by depreciation, inflation, and a number of other factors. But we do see a significant trend of small business on their choice going to measured service.

Representative **Wyden**. But what I asked you is are the small businesses in support of the specific proposal you filed with the PUC in Oregon? I would find that very hard to believe.

Mr. **Andrew Smith**. Congressman, it is like any other change in price. Some are and some are not. And generally the one who is going to enjoy an increase is not as excited as the one who is going to enjoy a decrease.

Representative **Wyden**. I thank the chairman.

Chairman **Packwood**. Congressman Wirth.

Representative **Wirth**. Thank you very much, Mr. Chairman.

Gentlemen, thank you for being here.

Could you first of all tell me if the rate increases that we see all across the country or requests for rate increases are as a result of divestiture?

Mr. **Andrew Smith**. Congressman, I will pass that to someone else. Our company has no filings in at this time in any of our territory.

Mr. **Wade**. My answer is not quite as clean. We have a case that is not yet priced that we are deliberating with the Illinois Commerce Commission. We do not have a specific filing yet, although we do have an inquiry to look at revenue requirements postdivestiture.

Mr. **Hayes**. Congressman, there has been a good deal of conversation about Texas. Since I am from Southwestern Bell, perhaps a few comments would be appropriate.

Representative **Wirth**. Does that constitute a yes or a no?

Mr. **Hayes**. It is going to be a no. That case in Texas has three parts. It is a $1.7 billion total filing. The three parts are very clear and very distinct. There is $754 million associated with access charges, replacement of toll contribution lost, and customer premise equipment contribution lost on the intrastate side.

We would not have that if we were not moving to a different pricing mechanism, but that is not associated necessarily with divestiture.

The other two parts are these: one, a request for an increase in depreciation cost of approximately $450 million.

Representative **Wirth**. And the third part?

Mr. **Hayes**. And the third part is business as usual, which is $502 million.

Representative **Wirth**. So divestiture did not have anything to do with the increase in Texas?

Mr. **Hayes**. As a matter of fact, it is very interesting. We are using forward costs, 1984 costs. That $502 million is only $20 million or so different from last year's case, and if it does have something to do with divestiture, it is this: we will no longer have our licensed contract and affiliated interest expenses as we have had in the past, and our new relationship with the CSO will be cheaper than the relationship of the past.

Representative WIRTH. Any of the rest of you have any reaction to that?

The reason I am asking is that we did an analysis in the Commerce Committee of the rate increases that have been requested and granted in 1983, and went through the rationale for those or to all of those States working with the State PUC's.

Let me say the following States cited the AT&T divestiture—in these proceedings in these States cited AT&T divestiture as one of the significant causes for a rate increase: the State of California, the State of Delaware, the District of Columbia, Indiana, the State of Maryland, the State of Missouri, New Mexico, Ohio—in fact, in the State of Texas that was cited in the discussions in front of the Texas State PUC—Oregon, Pennsylvania, South Dakota, Tennessee.

We just got the proceedings and went through and said what is the rationale.

Mr. HAYES. Not representations by us, I can assure you.

Representative WIRTH. Well, whatever it may be, the State PUC then cited that as a rationale.

Last year when Mr. Brown came down and testified before the subcommittee—and all of you remember the problem that we had getting examples of that—Mr. Brown said to us upward pressure on telephone rates as a result of today's competitive environment and inflation, not the modified consent decree, contrary to what we see in a whole lot of other statements.

Mr. Staley had said, contrary to that, "After divestiture we will receive no subsidy. Local rates will have to double in the next five years to bear their share of the cost."

Mr. Grossman, an AT&T spokesman in New York, said, "The long distance subsidy will be gone, and obviously the local companies will be under a lot of pressure to raise rates," and so on.

You will remember a lot of conflicting testimony between what Mr. Brown said—there will not be any pressure upward on rates because of divestiture—and a lot of local companies saying yes, there will be.

Now, the point of all of this, to go back to some of the discussion we had this morning, that there are three parts of the rate increases which I think you in part referred to. One is the whole access charge question, what happens at the FCC. The second is what goes on with the State PUC's and your requests to them independent of what goes on at the FCC. And the third is what goes on in terms of the asset allocation between the parent and you all.

Mr. HAYES. That is really wrapped up in the access charge part. Divestiture provides the timing, has telescoped the timeframe, but it is not necessarily directly related to the change in the pricing structure. That is the point.

Representative WIRTH. Is that right? In the divestiture process you end up with more debt and fewer assets. Your rates have to go up to be able to serve that local customer basically.

Mr. HAYES. Certainly.

Representative WIRTH. So, therefore, certainly the allocation of assets does have a lot to do with that.

Mr. HAYES. If that allocation—yes, it can have a lot to do with it.

Representative WIRTH. Mr. Chairman, my time is up.

I just wanted to point out that again, so that people do not have a hope that we are going to solve all of the problems here with an access charge bill, we are not going to.

You know, there are significant other problems of depreciation, there are problems of asset allocation between the parent and the operating companies and there are problems, you know, of how much are the State PUC's going to give you all when you come in for requests.

Do you all agree with that?

Mr. STALEY. Mr. Chairman, may I respond to Congressman Wirth since he quoted me on doubling of rates?

As you know, Congressman, I appeared before your subcommittee.

Representative WIRTH. I remember it very well, Mr. Staley. So do you, I know.

Mr. STALEY. You, of course, took me out of context at that time and also today.

Representative WIRTH. I am sorry.

Mr. STALEY. I said that the rates would certainly double, but they would double because of inflation, depreciation, interest, and other factors.

I would only point out that we received a recent rate cased award in New York State, and it amounted to 2.1 percent after waiting for 11 months of deliberations. So I would say that that is not exactly out of order, taking into account what is happening today.

Representative WIRTH. I would agree that that 2.1 percent is not, Mr. Staley, and I am sorry if you were quoted out of context last year and this year when I read the statement and tried to understand it. And my apologies if it was.

Mr. GUINN. Congressman, I would like to respond also, since you referenced California. We have two rate cases pending. One of them is an access charge rate case which is tied to divestiture. But I think we have to keep in mind that what is causing the local rates to go up, and what is creating the need for access charges, is the introduction of competition which took place a number of years ago. Competition has been eroding the revenues and taking the toll subsidy away from the local companies. Divestiture, as was said by John, will telescope that.

In terms of the other large rate case we have filed, it is for $1.248 billion. It is mostly depreciation, attrition and inflation recovery. I would think there might be some small amount of increased divestiture costs, but they do not deal with the toll rate subsidy which I think is your implication. What they deal with is the fact that when we had an integrated Bell System, we operated more efficiently than we will after divestiture.

For example, in my company we have got to put on nearly 300 procurement people to do the purchasing where that was done centrally by Western Electric before.

We do save some reduced costs, as John has pointed out, in terms of such items as the license contract costs. So the upward pressure of the pure restructuring of divestiture, I believe, is quite small relative to what we have been talking about.

Representative **Wirth**. Thank you, Mr. Chairman.

I would just like to point out that I think these gentlemen also have a major responsibility in the debt area, you know, to make sure that rates are going to go up if debts and assets are not properly allocated in the divestiture process. We made that point last year. I think it is appropriate to make that point again.

We do not have any control over that. You all do. On behalf of customers you have a major job to stand up to AT&T and make that case, which I am sure all of you are doing. I would just underline that again.

Thank you very much, Mr. Chairman.

Chairman **Packwood**. Congressman Lent.

Representative **Lent**. Thank you, Mr. Chairman.

I want to welcome the witnesses here, particularly Bud Staley of New York Telephone, who is an old friend and does an outstanding job in my State in providing telephone service.

I know, Bud, you do not like to be quoted out of context, and if you wanted to, you could quote Congressman Wirth out of context, and I am just going to take a little sentence from one of Congressman Wirth's recent speeches where he says, in referring to the FCC access charge:

> As written, the access charge order may provide the means for balancing the demands for affordable rates with the need to adjust prices to reflect an increasingly competitive environment. The FCC's plan minimizes the threat from bypass. It gives carriers the flexibility to formulate their access tariffs based on local conditions. It does not dictate huge local rate increases. The precise combination and amount of usage base and flat charges imposed on local customers will be set by the local telephone company subject to approval by the FCC.

So everybody is entitled to change their opinion.

Representative **Wirth**. Would the gentleman yield?

Representative **Lent**. This one is only 4 months old.

Representative **Wirth**. Mr. Lent, I agree completely with that statement. That is precisely the point that I have been making here, that no matter what we do on access charges, that is not going to solve the rate increase problem; that that relates to a whole variety of other elements as well, and we are fooling ourselves if politically we think that that is going to solve the problem. It is one part of a very complicated problem.

Representative **Lent**. If I may reclaim my time, may I ask the gentleman if that is the case, why did he introduce the Wirth bill? Why did you this year introduce the Wirth bill to reverse the access charges, if you said in that statement that you thought the access charges were going to work out and be reasonable?

Representative **Wirth**. The access charges were not working out and being reasonable. I think that that came after we had negotiated very heavily with the FCC at the turn of the year trying to get them to get a better balance. And as I have pointed out in a discussion with the Chairman of the FCC this morning, we were trying to get that balance between economic efficiency and the social goals, and we did not get as far as we wanted to get.

Representative **Lent**. OK. Well, I never quote anyone out of context anyhow.

But, Mr. Staley, you said in your prepared statement that prohibitions on bypass as contained in both the Dingell and Packwood bills are unenforceable and unworkable. Would you explain what you meant by that?

Mr. **Staley**. Well, I meant that there would have to be some way of actually detecting the bypass to begin with. We have, when people order service—of course, you are talking about fraudulent bypass—when they order service we do not have the slightest idea of why they are ordering service. They may be ordering it to provide additional features on their own service, or they may be providing different operations with respect to their business. We have no way of determining why they are ordering that service.

I guess the best example of having difficulty in trying to determine and enforce illegal interconnection is what exists today. We have years of experience with this. We have had, for instance, people illegally interconnecting their telephones for quite some time. With the action taken whereby these telephones can be bought now, we have many, many illegal interconnections. We have spent hundreds of thousands of dollars on testing equipment and on testing hours, and it is absolutely impossible to detect illegal interconnections. There is no way to enforce it.

Representative **Lent**. We have had a lot of testimony—I think you mentioned it today in your prepared statement—the upcoming proposal of New York Telephone to the New York PUC for a lifeline rate.

Could you tell us how that would work and how can we be assured that the truly needy will be the beneficiaries of such a system?

Mr. **Staley**. Well, the lifeline rate that we are proposing will be a flat $5 a month charge, and in the measured areas there would be zero calls allowed. We have, of course, measured service in the bulk of our territory. In those areas where we do not have measured service, we would establish an equivalent service at a flat rate. We would propose that we not be the ones, of course, to set the criteria. There are many agencies in existence today—State, local, Federal, private agencies. We would expect them to determine the criteria, and this would be a very workable plan, from our viewpoint.

Representative **Lent**. Could you just tell us very quickly how long your company has had measured rate service in New York City?

Mr. **Staley**. Well, we have had measured service for over 30 years, and it is mandatory in New York City. I spent 28 years with Illinois Bell. We had measured service in Chicago for over 30 years.

And in reference to the comment about its effect on small businesses, I know of no cities in the country with more small businesses than Chicago and New York.

Representative **Lent**. I thank the gentleman.

Mr. **Guinn**. I might add, Congressman, that we also have measured rate service for small businessmen in California, and it seems to be working satisfactorily.

Chairman **Packwood**. Congressman Gore.

Representative **Gore**. Thank you very much, Mr. Chairman.

I would like to add my welcome to our witnesses here today. This is an issue that has caused as much concern in the State of Tennessee as any issue that has come down the pike in a long, long time; and none of you should suffer the illusion that it is going to die with a whimper in the Congress.

In my judgment, the legislation pending before these two committees will pass in the Congress. There undoubtedly will be some amendments, but it will pass substantially in the form that it now has, in my judgment.

Now, we simply cannot—I am sure you have heard a lot of statements already this morning about how strongly people feel about it, and I want to add to the weight of those statements, but I want to associate myself with them.

We cannot allow the kinds of rates increases that have been proposed to take place. It just cannot be allowed. And whatever needs to be done and has to be done to prevent that, we are going to do it on an urgent basis.

Now, you have all endorsed the FCC's access charge decision, is that correct? You all agree with that, and you have defended it as economically rational. I have studied accounting——

Mr. ANDREW SMITH. Congressman, there were a few qualifications to that. I think I made it quite clear that we have some serious concerns about the present form of docket 78-72, but the philosophy of its approach as originally established appeared to be workable.

Representative GORE. Well, now, do you think it is economically rational to take the contribution of the long distance companies down to zero for the lines, poles, and equipment in the local service areas?

On what economic principle is that based?

Mr. ANDREW SMITH. I do not quite understand your question.

Representative GORE. To put it all on the consumer on access charges, is that rational?

Mr. ANDREW SMITH. Of course, the charges that are paid by the carriers, they actually still pay charges. They do not get their connections for nothing.

Representative GORE. Not for the jointly used plant.

Mr. GUINN. I thought I understood, Congressman——

Representative GORE. Let me stay with the same respondent here.

They are not paying for the jointly used plant under that decision, are they?

Mr. ANDREW SMITH. At the end of the 5-year period under 78-72 that does phase to the end user, that is correct.

Representative GORE. Under what economic theory can that be described as rational? I mean joint cost accounting is more of an art than a science. But I do not know who in the world has ever taken the position that it is rational to go 100 percent to one side and zero percent to the other.

Mr. ANDREW SMITH. I think the rationale for it, Congressman, is that fundamentally the end user charges today are seriously below the cost of providing that end user facility, and the shifting period is simply a transition period to allow that full cost coverage to be picked up and covered on the basis of what it actually costs to provide that service.

Representative **Gore**. But that does not answer the question, with all due respect, and I interject because our time is so limited. It still does not answer the question. You have got the same facility being used by two services.

Mr. **Andrew Smith**. The facility today, however, for the end user, Congressman, is seriously underpriced.

Representative **Gore**. That is not my question now.

Mr. **Andrew Smith**. But that is my answer.

Representative **Gore**. Under this decision you have got the same equipment, the same facility used by local calls and long-distance calls. Now, we can argue about what percentage should be allocated between the two services, but to take the position and defend it as economically rational as if it comes out of some textbook, to take the position that it is rational to take all of it off of the long-distance calls and put all of it on the consumer, I know of no justification whatsoever for that.

Mr. **Andrew Smith**. Let me make it clear, Congressman, that under the monopoly considerations that we originally operated and developed universal service in this country and which we supported and did not offer to change—somebody said this was not our idea, this whole change.

Representative **Gore**. But you have endorsed it.

Mr. **Andrew Smith**. Let me finish, if I may. May I finish?

Representative **Gore**. Yes, please.

Mr. **Andrew Smith**. As we move from a monopoly environment with costs arbitrarily distributed for social purposes to what is alleged to be a fully competitive environment—and that is the philosophy that is expressed in public policy at this point—this is an absolute necessity.

Representative **Gore**. It is not fully competitive. It is partly competitive and partly exploitative. It is becoming competitive in the long-distance area, and the consumers are to be exploited in order to give the long distance providers a free ride so they can come in and use the joint facilities free of charge.

Mr. **Andrew Smith**. Congressman, I think you overlook some of the other things available to the end user station. Costs have come down sharply for both the residence customer and business customer; expanded service is available. I think your comparison is unfair and inappropriate.

Representative **Gore**. Well, no service at all is going to be available to a lot of rural customers and a lot of residential customers that cannot afford it. In my congressional district and in the State of Tennessee, if this 128-percent rate increase—and I apologize, Mr. Clendenin, that my time has run out, and I have not had an opportunity to have some questions directed to you—but if that increase goes through or anything resembling it goes through, the percentage of people without telephone service is going to jump dramatically and the quality of their service is not going to be very good at all.

Chairman **Packwood**. Let me remind the members we will have a second go-round on questions. Try to hold them down to 5 minutes on the first round, because we have so many of us. We will come around and around as long as people want to ask. Let us move on to Congressman Corcoran.

Representative **Gore**. Thank you very much, Mr. Chairman.

Representative **Corcoran**. Thank you very much, Mr. Chairman. Let me say at the outset I regret that I was unable to be here this morning to hear the distinguished panel of public utility commissioners, and I also regret that I probably will not be able to participate in the hearings through their duration today and tomorrow. But I am very appreciative, as I know everyone is, that the respective Commerce Committees in the House and Senate are conducting hearings on this problem at the moment.

Let me also say in passing, Mr. Chairman, that the impression might be, I suspect, that the public utility commissioners who participated in the panel this morning are relatively agreed as to the impact of the various legislative proposals which are pending in both the Senate and the House. However, I can assure you that they are not uniform. I know that the Illinois Commerce Commission has many misgivings about the legislation that is pending.

I might also say that while there is a concern about the impact of this decision from the Federal Communications Commission and other pending matters on a nationwide basis, my own particular interest is relative, of course, to my district and to the State of Illinois.

And I am happy to note that Orm Wade, the president of Illinois Bell, is with us, and with your indulgence, Mr. Chairman, I would just like to focus my questions on the Illinois situation.

It is my understanding, Mr. Wade, that the purpose of the Universal Service Fund, which is created in both the Packwood legislation and in the Dingell-Wirth legislation, is to provide a subsidy to rural and residential telephone customers.

So my first question relates to the fund itself. I gather from a rather cursory reading of the legislation that the money would be provided from a surcharge that would be placed on the carriers and on their customers. And in that regard, I would like to know if you have had an opportunity to evaluate the legislation and whether or not you could tell us how much the carriers and customers in Illinois will pay each year into the Universal Service Fund?

Mr. **Wade**. Congressman Corcoran, in a cursory way we, too, have had a chance to look at it and not comprehensively. My understanding is the surcharge would be applied to the interexchange carriers providing service, and my assumption is that that would then be passed on to the customers who are using that service.

I believe the amount would be measured in probably the tens of millions of dollars, something like that.

Representative **Corcoran**. Do you have any idea how much Illinois might receive in return from that Universal Service Fund?

Mr. **Wade**. The only numbers that I saw were in the $300,000 range.

Representative **Corcoran**. Now, let me see if I understand this. You are saying that the amount of money that our consumers would have to cough up to this fund is in the millions, and the amount of money that we would get in return is in the range of $300,000?

Mr. **Raymond Smith**. If I may, Congressman, Pennsylvania is very similar in size and makeup to Illinois, and I happen to have the Pennsylvania figures which are about $140 million paid out and $2.6 million coming back. So many of our things are similar, it might be on that order.

Mr. **Wade**. There is an issue, I think, that was discussed earlier when you were not here, Congressman, and that is the issue of the universality of service really being also a function of some nationwide concern about the reachability of telephones everywhere across the country. We certainly recognize that.

We do not contend that this is purely a regional issue, but I do think it is important to understand that there are some important differences.

Representative **Corcoran**. Let me ask you further with respect to the creation of the fund, might it not be better to have a state fund within which you could develop the internal flow of the subsidies which we are trying to correct?

We are trying to resolve this change that is taking place. Might it not be better to do it within each State rather than on a nationwide basis?

Mr. **Wade**. I think that is an option that needs to be explored more fully. In fact, that was suggested earlier today by another witness.

I also support the concept of focused, targeted relief in fairly defined and fairly narrow ways.

Representative **Corcoran**. As you well know, the intention of the legislation before us is to provide some subsidy assistance to the rural and residential customers, and so I have a question in that regard.

What will be the impact on rural customers in Illinois? How will they benefit from the Universal Service Fund? And how, for instance, would a poor family in Chicago benefit from this?

Mr. **Wade**. Well, I am afraid we really cannot answer those specific questions yet because there is still so much to be worked out in the administrative detail of just how it would work and just exactly who benefits by what amount.

Obviously, in a broad-based subsidy or exchange of fund scheme there are going to be people who are providing support to others that makes no economic or rational sense. People who are on welfare will probably be supporting people who are very, very handily able to pay it themselves.

Representative **Corcoran**. Thank you.

Chairman **Packwood**. The present policy—and I will direct this, Andy, to you—the present policy on separations and settlements is one of long standing, right?

Mr. **Andrew Smith**. Yes.

Chairman **Packwood**. Under that policy, many States probably collect more money from their long-distance customers, and it is paid out to residential and rural customers in other States, is that correct?

Mr. **Andrew Smith**. That is correct.

Chairman **Packwood**. We had the PUC Commissioners today, and I believe the FCC says that the present separations and settlements policy does not differ significantly from the bill that either

Congressman Wirth and Congressman Dingell have introduced, or I have introduced.

Mr. **Andrew Smith**. I heard that statement, Mr. Chairman. The problem with it is, of course, that while the policy may be very similar the actual amounts of dollars appear to change significantly under this proposed legislation, PNB, for example, under the existing separations and settlements, is about a zero company, no in or out flow. Depending upon which of the funds you look at, we can range up to as high as a $25 million annual outflow from PNB under this proposal.

Chairman **Packwood**. If it is going out of Pennsylvania and New York and California and Oregon and Washington, where is it going to?

Mr. **Andrew Smith**. Florida.

Chairman **Packwood**. All of it is going to Florida.

It cannot be going out of every place and not into some place.

Mr. **Andrew Smith**. That is a zero sum game, and there were two mentioned, I believe, here, Florida and Alaska, which are a couple, and I am sure it bears investigation. But that is our particular situation.

Mr. **Staley**. Senator, may I also comment on that?

Chairman **Packwood**. The reason I want to ask Andy a few more questions is because I have got to go to vote, and I want to follow some sequence on this.

A year and a half ago, when you and I were working closely on S. 898 and I was meeting with Charlie Brown, this was our divestiture bill that passed here, and it passed before the consent decree and then sort of died in the House and became moot.

You will recall at that time we were aware that the FCC was working on their access charge concept, and we were a little worried that they might change it, and so we wrote into S. 898 in essence what is in the provision of my bill now.

We statutorily required the FCC to continue their subsidy policy, and at that time that provision was acceptable to AT&T and the operating companies. In fact, as you and I specifically recall, they had a fair hand in drafting it.

I am curious what has changed in the year and a half?

Mr. **Hayes**. Bypass for one thing. That is the biggie.

Chairman **Packwood**. Bypass, Mr. Hayes is saying. It was not as bad then as it is now.

Mr. **Andrew Smith**. Of course, in the plain size of the competitive carriers, the other common carriers have changed very significantly over that period of time.

Chairman **Packwood**. Well, it seems to me you have two questions. One is the philosophy of the subsidy and the argument does it go out of Illinois and into Arkansas, does it go out of New York and into Florida, where does it go. And that is an argument that we face in this Congress all of the time. It does not matter if it is revenue-sharing formulas or anything else. Does New York win, Oregon lose, or vice-versa. And that is always a legitimate question.

But it would seem to me at some stage there has got to be some operating companies that gain and some that lose, if that is going to be the issue.

Mr. **Andrew Smith**. I guess the real question that is my personal concern, Mr. Chairman, in this whole arena is the size of the proposal. It appears to us that to meet the need that you are expressing in the philosophical approach to your legislation, that of taking care of those that cannot afford to pay for telephone service, but certainly based on the rather detailed study that we have, the size of that problem is significantly less than what the answer would be provided from your proposed legislation.

The other aspect that is of great concern, I think, to all of us is the bypass problem which is increasingly sapping revenues and further aggravating the problem of that person who cannot pay for their telephone service.

Let me just go one step further, if I may. I wonder whether or not there is not a more limited approach to legislation bringing those two elements together that would be worthy of consideration for the committee.

Chairman **Packwood**. It may be. We are going to have all of August to work on this before we start our markup, and all of August is not all that long a period of time when we start our markups in September.

But I want to come back to the philosophy. One, you are all worried about a bypass. I understand why you are worried about bypass. We are worried about bypass, because if we go ahead with a subsidy system and we drive people off the system that is going to be the subsidy, there is no subsidy, and we have not achieved the goal that we would like to achieve. And all we have succeeded in doing is destroying the long lines and having a lot of profitable bypass systems and people who cannot afford rural telephones. That is something I do not think any of us want to reach.

If we can reach the bypass problem, if the FCC says yes, by and large we can reach it, we can find a way.

Mr. **Andrew Smith**. Identification?

Chairman **Packwood**. Yes. Then it seems to me that solves your bypass problem. And then you come back to the philosophical problem of should we be using long distance charges to subsidize residential and rural—long distance, whether they use your lines, or a private satellite system, or their own lines in house.

If we can solve that, should we have the subsidy, and that comes down to the concept of user charges versus subsidies.

Mr. **Andrew Smith**. And the size, I think.

Chairman **Packwood**. I understand that.

Mr. **Andrew Smith**. I really feel that the action that was taken by this committee in the legislative proposals had a very significant impact on the change in the FCC's 78-72. We are disappointed. It kind of went both directions. It helped the consumer on the short term, but on the long term may hurt them more seriously than before.

Chairman **Packwood**. Let me give you just one word of advice, and then I am going to go, and there is no one else here to ask you questions, and I think we will let this panel terminate.

I think you play a very dangerous game if you cite these figures about $100 million out of New York and $6 million in, because if that is true, where the heavy concentration of long-distance users is located, which may be in 8 or 10 States, then at least in the

Senate you are playing a losing game, because every one of those other 40 or 42 States are going to say you mean to say that we can get all of this money from New York and Pennsylvania and California on their long distance?

I think it is a dangerous game for you to get into, because inevitably there are more small rural States than there are big, immense urban centers.

I have got to stop because that buzzer means I have got 7 minutes to get to a vote, and I have no more questions of the panel.

Again, you have been very, very tolerant.

We will adjourn the hearings for about 15 minutes, and I will get back for the last panel.

[Recess.]

Chairman PACKWOOD. Let us come back to order and take our last panel, if we might.

Mr. Nehring, Mr. Snedaker, Mr. Copsey, Mr. Ware, and Mr. Keen.

Have you fellows been listening all day? I hope you were not planning to catch the 4 p.m. plane back to Arizona.

Mr. NEHRING. I would not miss tomorrow for anything.

Chairman PACKWOOD. Why do you not go ahead, Mr. Nehring?

STATEMENTS OF ROLLIE NEHRING, PRESIDENT, ARIZONA TELEPHONE CO.; ROBERT SNEDAKER, PRESIDENT, UNITED TELEPHONE SYSTEM; EVAN COPSEY, PRESIDENT, FIDELITY TELEPHONE CO.; LAWRENCE WARE, MANAGER, GARDEN VALLEY TELEPHONE CO.; AND JACK KEEN, PRESIDENT, WESTERN NEW MEXICO TELEPHONE CO.

Mr. NEHRING. Thank you, Mr. Chairman.

My name is Rollie Nehring. I am president and majority stockholder of Arizona Telephone, headquartered in Phoenix, Ariz. We serve 10 areas in Arizona. We are a prime example of a small company serving isolated high-cost areas, which involve some 5,300 square miles about the size of the State of Connecticut within which are located 1,450 customers with about 1.8 per route mile of line.

I appear today as an individual, not representing a trade association, although we are members of a number of the trade associations, both national, regional, and State.

I am a member of the USITA board of directors, and a member of the executive committee which has tussled with these policy problems frequently over the last year.

I appreciate the opportunity to testify. This makes it No. 5 for me before a combination of the Senate and House committees starting back in 1976. I hope we are nearing that end of the cycle in the 7-year average life of major legislation.

Due to industry involvement and familiarity with the exchange operations of many other companies, I believe I can speak for many of the other small companies serving similar areas to what we have.

In Arizona and across the country and particularly in the West, we do have these isolated, remote areas. Perhaps Havasupai is our best known example of universal service where 350 native Americans are served at the bottom of the Grand Canyon.

My written testimony addresses S. 1660 only because I did not receive the House bill in time to get the statement on its way, and I limited my comments to S. 1660 to basically policies and objectives of the bill.

I see no reason after having read the House bill why they cannot be blended both philosophically and in most details. And I state at this time that I speak in support of both bills and the policies and objectives they set forth.

I will be happy to answer any questions regarding the details on any of the bills the Congressmen and Senators may choose. From the many questions raised earlier, it remains apparent that there is a lot of haze about the impacts which directly will affect the success of the deliberations on the resolution of philosophy. Therefore, perhaps I could use our small operation as a bit of a model to attempt to move away from the discussions of billions and talk about some of our actual 1981 operations to identify impacts of a high-cost company.

Our investment per access line is about $3,500. If anyone would like to later question how we arrived at those amounts or whether we have gold plated, I would be glad to answer questions on that.

We are allowed a rate of return based on revenue requirements, and for the investment we have, our revenue requirements for 1981 were $1,341,000, which equates to about $100 per month per access line. That is what it costs us to operate in these areas. And it resulted in a rate of return of a little over 9 percent, which is quite acceptable.

Now, of that $1,341,000, our local revenues only generated $157,000. That is still an average of $11.70 per month per access line. Our toll, both intrastate and interstate, amounted to another $549,000, which is $40.83 a month, so that is what our customers generated, basically a toll of $53. Well, obviously if our cost is $100, there is $47 coming from somewhere else, and that is an amount of $635,000 that comes from the support, or if you will, the subsidy under the present Ozark settlements.

The question then is where does the $47 come from in the future? If we pass that on to the customer, he will be paying that amount plus the $11.70 average now, for a total of $58, and we simply will lose many of them, if not all of them.

So in conclusion, I would like to say I support the policies and objectives regarding universal service of both bills. I disagree with the shift all of NTS costs to the customers. It should be shifted to the carriers on a usage sensitive basis.

I support the provisions of the universal fund for support of the low-density/high-cost areas. I feel the Federal and State regulations should be consistent, but the State regulators really should be left with a maximum of flexibility.

There is one other item regarding relief, and that is the double whammy of low-density toll routes which are more expensive, and if we are to pursue.

Chairman **Packwood**. I have got to ask you to wrap up, Mr. Nehring.

Mr. NEHRING. Cost-sensitive pricing there, we are in trouble, and the averaging there should be looked at very hard.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF ROLAND G. NEHRING ON BEHALF OF THE ARIZONA TELEPHONE CO.

Mr. Chairman and Members of the Committee, my name is Roland G. Nehring. I reside in Phoenix, Arizona and am the organizer, principal stockholder and president of Arizona Telephone Company. My formal educational background consists of a B.B.A. in accounting and a Degree of Law obtained from the University of Wisconsin. My experience in the telephone industry began in 1961. In 1968, I started Arizona Telephone Company to serve unserved areas in the state of Arizona. Our operation presently consists of ten exchange areas serving 1450 customers and is a prime example of high cost low-density areas located in the more remote areas of Arizona with 1.8 customers per route mile of telephone plant. Our best known exchange operation is located at the Havasupai Indian Reservation at the bottom of the Grand Canyon where approximately 350 native Americans reside.

Thank you for the opportunity to testify at this hearing and to express my overall support for the policies and objectives of the Universal Telephone Service Preservation Act of 1983. I have had occasion to testify a number of times in the past starting with the initial hearings before Congressman Van Deerlin's committee on September of 1976 and concluding most recently with testimony before this committee on June 16, 1981 concerning S. 898.

I've tried to articulate through all these years the concern of the small companies serving the high cost low-density areas for both constructing plant and maintaining it to ensure qualify of service at reasonable and affordable rates. That concern for proper pricing for basic telephone service has not changed since 1976 as evidenced by a quote from my statement involving that hearing as follows:

"If, therefore, we are to change our pricing approach to usage pricing—the cost of providing the service, it will preclude many of our customers from service due to the monthly rates required and the charges for maintenance calls to their specific site. The end result, I feel, is that we will lose customers and be forced out of business."

My concerns in 1976 involved the prospects of the new competitive entrants selectively skimming our best customers and our concern over loss of the customer terminal investment base which would result in local rate increases. By 1981, while testifying on S. 898, my concern was directed to the threatened replacement of current settlement procedures by access charges with the plea that the access charges must be adequate to replace the revenues lost through the change in settlement procedures. That evolutionary process in re-structuring of the telephone industry has now developed into full scale revolution.

During the latter testimony, I estimated that our local rates could increase by as much as $20.00 per month. In the following testimony, to better understand the pending economic impacts on our small company rural operations, I will utilize our own company's statistics. Hopefully, this will be of value in testing the reasonableness and appropriateness of the policies and objectives contained in this Bill. With each passing year and series of hearings, the impact on our customers local rates becomes more adverse and could be approximately $40.00 more if the FCC system of access charges are adopted.

The common carrier segment of the telephone industry has asked through the years that Congress pass legislation to establish clear national policy regarding telecommunications service and particularly universal service. Our industry has never been able to reach concensus within its ranks on how universal service was to be achieved for all of the diverse operations in this nation with the advent of competition. I support the approach of this Bill because it clearly sets forth the intent of Congress regarding universal basic telephone service and that high monthly flat rates on the end user should not be permitted since that would be detrimental to the survival of universally affordable telephone service. S. 1660 places its emphasis on usage rather than flat rates.

With public policy so clearly stated, the industry and its regulators should now be able to work out the details that will ensure that this country maintains its infrastructure of basic telephone service. During testimony on S. 898 other telephone witnesses stated that legislation would raise rural rates appreciably and to a greater extent than urban rates, although those increases would not happen all at one time. There was also general support for equitable access charges for connecting interexchange channels to the local exchange facilities of a carrier as a means of replacing revenues lost through changes in the settlement formula. When I referred to a revolution in our industry, it is clearly demonstrated that in just two years, it is now commonly recognized that drastic increases in rural areas and for residential service are imminent and furthermore, that the settlement revenues have not only been diminished but will be totally replaced by access charges. Unlike the contemplation of usage access charges under S. 898 however, the FCC under Docket 78–72 and 80–286 placed all of those access charges for non-traffic sensitive plant on the end user. This Bill which establishes an access charge system based on usage is fair because it gives the user the option of "buying" as much service as he or she desires. A high flat rate on the end user as a primary means for local telephone companies to obtain their revenues does not leave the end user with any choice of payment whether they are heavy or light users.

Probably the only semblance of a natural monopoly still existing in the telephone industry is the facilities of the exchange companies since they are still required to serve everyone whether they be large or small users and are looked upon as the providers of last resort. Those who selectively bypass exchange facilities for their particular economic or other reasons and cause migration of users and revenues from the local exchange, either directly, indirectly, or on a nonconnected basis should pay some support for maintenance of basic communications. Even non-connected private systems will "leak" transmissions to the local distribution networks across the nation. S. 1660 addresses the bypass problem which has troubled the larger telephone companies for so long.

This Bill addresses a very complex situation. The answers to obtaining lost revenues via access charges on one hand seems to be very simple and yet it raises very difficult problems in maintaining universal service at the same time. The complexity of simple answers and the raising of difficult problems is akin to this nation's financial difficulties where budget deficits must be weighed against higher interest rates and inflation.

For years the hue and cry has been cost causer—cost payer. We have now seen the FCC position emerge to use flat rate charges on the end user regardless of usage, simply on the basis that the nontraffic sensitive plant is there and available. Placing all access charges on the end user as the cost causer is not pure or clean. Why should someone who is a few blocks from our switching center pay the same monthly access charge as someone who is located many miles away and has caused substantially more investment to tie him to the network?

This Bill fortunately looks to usage access charges to provide the funds for most of the universal service costs in excess of 110% above national average costs and perhaps it should provide for all excess costs. The Bill utilizes "pooling" which is essential to the survival of universal service in high cost areas, particularly those areas served by small companies who do not have the size for diversification or affective averaging within their own operations. For example in Arizona, Mountain Bell can average their low density areas with the Phoenix and Tucson urban operations. Arizona Telephone cannot do so and could be placed in a position where our rural exchange rates by comparison to an adjacent similar density Mountain Bell exchange could be many times higher, even though we are operating at our efficient best. Arizona Telephone should not be penalized for having extended universal service in the first place, simply because it has no high density areas to average into the low-density, high cost areas. Pooling will serve to normalize charges not only within general exchange service areas within a state but within the entire nation.

As I have previously commented, it is absolutely necessary that all present revenue requirements will be satisfied on a usage sensitive basis rather than a flat rate and end user basis in order that universal basic telephone service can survive. Under the FCC proposal, the pendulum has swung totally from the point where long distance revenues were subsidizing local rates to that where local rates are now subsidizing long distance. The interexchange carriers will be allowed free access to our non-traffic sensitive plant since our end users will be paying that obligation. I see no reason why the interexchange carriers and private systems should not pay a significant portion of the NTS plant costs based on a usage basis. The plant is in place for the interexchange carriers to access and utilize in making a profit. If the existing local facilities were not already in place, those interexchange carriers would have to build their own distribution facilities at considerable cost to them.

Congress must confirm the policy for continuing the support payments, revenue sharing, or if you will—subsidies for the rural areas to ensure the survival of Universal Basic Telephone Service. The standards, formulas, and rules developed to-date are hazy and at best very difficult to understand even for members of the telephone industry. Please permit me to summarize the bottom line costs and revenue requirements of our operations for the year ending 1981.

Our net investment for rate-making purposes was $3,884,000 on which we earned $363,700 before payment of interest. That is a 9.4 percent rate of return. The revenue requirements for that year were $1,341,000 or about $100.00 per access line per month. Our customers paid an amount of $53.00 per month for local and toll usage. That means that $47.00 per month came from the settlement process to meet the revenue requirements which resulted in our 9.4 percent rate of return.

If we were to charge our customers another $20.00 per month for interstate access, their total monthly payment increases to an average of $73.00. If we then also mirror the federal access charges with state access charges, another $20.00 per month must be added to our customers costs, for an accumulated average monthly total of $93.00 per customer. At this point we have almost met our revenue requirements of $100.00 monthly, but we will have lost much of our customer base due to unwillingness or inability to pay the increased monthly payments. Therefore, I reiterate that Universal Service cannot survive in our areas unless the policies of this Bill are adopted.

Without legislation, there will be no incentive for big or small companies to provide good service in the rural areas nor to upgrade to the latest state of the art. We have been down the road before where extremely high aid in construction costs made it impossible for rural customers to obtain telephone service. The REA program was developed for that reason. We'll be moving back to that situation without legislation. The FCC access charge plan would discourage utilities from not only extending service but from upgrading it and adequately maintaining it as well, The parity of service between rural and urban America will have been lost.

Finally, the rural customers face a double "whammy" due to the proposed deaveraging of toll routes. Our areas are served via low density toll routes which under deaveraging will result in greatly increased rates. For the good of all America, averaging should be maintained.

There are a number of housekeeping matters that involve language clarity that I am sure will be addressed by othrs testifying on this Bill and by the Committee Staff so I will not dwell on those items. It is imperative that Congressional national public policy regarding universal sevice be established *now*. In my opinion, the FCC has strayed too far and has had court reversals even on some of its decisions. The state regulators and the telephone companies need that policy established immediately since many are awaiting your decision before adopting state plans that will mirror the federal rules and policy.

Jurisdiction questions have been resolved by the Bill and state and federal regulators are now placed in a position where they can establish the mechanisms and participate in the joint decisions affecting the Universal Basic Telephone Service of this nation. I am certain that there is sufficient talent within the industry to work with the regulators to ensure that the best telephone system in the world will be preserved. Thank you.

Chairman PACKWOOD. Thank you.

Mr. Snedaker.

Mr. SNEDAKER. Chairman Packwood and Chairman Dingell, I appreciate the opportunity to appear before this joint hearing. I am here to represent the views of United Telephone Co. as well as the views of the United States Telephone Association, an independent telephone association which has 1,432 members.

As indicated in my written statement, we generally support the FCC access charge plan. The plan is a reasonable, workable, and economically sound means to resolve the problems created by the introduction of competition into the long-distance telephone market.

It is United's and USITA's position that the modification voted on by the FCC to limit the end user charge to residential customers to a maximum of $2 per month yesterday will help reduce the impact in the first year of access charges to a level that should not be burdensome, and which in my opinion would not adversely affect universal telephone service in this country.

The lengthening of the transition period to 6 years will likewise soften the impact through the period.

As you know, the FCC spent approximately 5 years examining all of the issues, compiling an exhaustive record, and considering the views of all interested parties before reaching their decision. USITA and United both participated in that process.

I might add that during the process we learned quite a bit and did modify our position. We became convinced that the recovery of nontraffic sensitive costs from end users should ultimately be made on a flat rate basis although the transition mechanisms are very important to consider.

Universal service obviously is a very important part of our consideration. It is in USITA and it is in United. The ability of customers to place calls to all other subscribers certainly enhances not only our ability to conduct a viable business, but contributes to our national overall economic, social and political development.

In order to sustain universal service in a competitive telecommunications environment, though, the contributions, which could be justified only in a monopoly area—that is, the subsidies—must be substantially reduced, and the price for services must be based on their cost.

Thus, we believe the FCC access charge plan is needed to help to preserve universal service for the long term, which was pointed out by the earlier panel, and is not a threat to universal service. It will not produce increased revenues to local telephone companies. Indeed, the net impact of access charges on all customers on a nationwide average basis under the present setup would be zero. It is just a shifting from one group to another.

Long distance rates were predicted today, and we will agree, will probably drop 15 to 40 percent, both interstate and intrastate. In fact, there are companies in the Bell System—Ohio Bell, for example, has filed for a 40-percent reduction in intrastate long-distance rates within that State.

Telephone bills paid by many customers may not increase as much as feared by some, and that was discussed today also. We estimate for those customers who generally make $20 to $30 per month in long distance, it would come out about even, and obviously, those making more would come out ahead.

The universal service fund contained in the FCC's access charge plan will provide revenue support to high cost companies to protect their customers against extraordinary rate increases. The high cost factor recommended by the Joint Board to fund the support is estimated to total approximately $1 billion and maybe more as a result of yesterday's action by the FCC.

The FCC is developing, as we heard this morning, a postimplementation monitoring procedure that should enable them to make any adjustments that are appropriate. And lifeline service, which was discussed, we believe is aimed at the people who need and who will benefit from that particular option.

So we respectfully urge Congress not to enact corrective legislation at this time. Some observers believe there is an immediate problem caused by several recent large local cases mentioned here today, but as was questioned today, these requests reveal that a lot of the revenue requirements are not generated by the pending implementation of access charges, but are attributed to other factors.

So in conclusion, we think that the plan that the FCC has come up with will work. It will enable our industry to continue to be an efficient provider of telephone service to the public in the future while permitting customers to enjoy all the benefits of competition in a deregulated telecommunications environment.

[The statement follows:]

STATEMENT OF R. H. SNEDAKER, JR., PRESIDENT, UNITED TELEPHONE SYSTEM, INC.

My name is Robert H. Snedaker, Jr., and I am President of United Telephone System, Inc. I am also First Vice President of the United States Independent Telephone Association (USITA). There are 1,432 Independent Telephone Companies serving 59 percent of the nation's geography, and 35 million telephones, with 192,000 employees and $41.9 billion invested in telephone plant. My Company provides certain managerial, administrative and professional (e.g., legal, accounting, engineering, etc.) services, on a consolidated basis, to the 22 operating telephone companies, doing business in twenty states,[1] that comprise the "United Telephone System." A United States map, with the UTS operating areas shaded, is attached hereto as Exhibit No. 1. The UTS companies are subsidiaries of United Telecommunications, Inc., a Kansas-based holding company.

UNITED TELEPHONE SYSTEM

The United Telephone System is the second-largest Independent (non-Bell) telephone system in the United States. At year-end 1982, the UTS companies served almost three million telephone access lines in approximately 3,000 rural and suburban communities. The UTS companies had $5.35 Billion invested in Telephone Plant, employed 25,560 persons, and generated $1.83 Billion in local and long distance revenues. A copy of page 44 of the 1982 Annual Report of United Telecommunications, Inc., which gives certain UTS statistics, is attached hereto as Exhibit No. 2.

As a major provider of basic telephone service in this nation, we are vitally interested in the preservation of universal service. Our customers are not just our primary source of income—they are our primary concern in our management and operations decisions, as well as in the positions we take on proposed telecommunications legislation. We want and need to be able to price our service within the range of affordability of our telephone customers; when customers "drop-off" or bypass the network for economic reasons, we lose too.

ACCESS CHARGE PLAN

Thus, I am most appreciative of this opportunity to share with you our reasons for supporting the basic tenets of the FCC's Access Charge Plan (Docket No. 78-72) and, at this time, opposing legislation which would impede its implementation. I must observe, in that regard, that the FCC has professionally discharged its responsibility as the executive agency expert in telecommunications matters by conducting an exhaustive five-year investigation, giving all interested parties repeated opportunities to make their views known, compiling a complete and open record, and reaching an informed judgment based both on the evidence and sound economic principles.

The FCC substantially adopted the general concepts espoused by USITA and UTS and, accordingly, we strongly believe that the Access Charge Plan is the best possible solution to the complex problems resulting from the introduction of competition into the intercity market. Thus, we respectfully urge Congress not to disregard it lightly. In particular, we urge you to give the FCC's Access Charge Plan an opportunity to work.

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[1] Arkansas, California, Florida, Indiana, Iowa, Kansas, Minnesota, Missouri, Nebraska, New Jersey, North Caroline, Ohio, Oregon, Pennsylvania, South Carolina, Tennessee, Texas, Virginia, Washington, and Wyoming.

SUBSIDIES

We believe that access charges are necessary in a competitive environment; that the existing division of revenues and settlements process (and resulting cross-subsidies) was justifiable only in the monopoly era. The controversy arises when the system of subsidies long-embodied in the toll settlements process is abandoned, and the true cost of service is assessed against the cost-causers.

The subsidies embodied in the current toll settlements process (the Ozark Plan, contained in the NARUC/FCC Separations Manual) result from the allocation of the investment costs and associated expenses of Non-Traffic Sensitive plant (or the "local loop"—the dedicated facility between the telephone company's central office and the customer's premise—see Exhibit No. 3) between local and toll services. The current allocation, (known as the Subscriber Plant Factor), which has been frozen by FCC order since April, 1982, assesses about 3.3 times the amount of NTS costs to toll service than relative use would reflect; the excess revenues thereby produced constitute a non-targeted subsidy to local rates.

Such subsidies cannot be justified in a competitive environment; not only would they distort the competitive process and encourage uneconomic plant investment, but they are an unsatisfactory means to address what is essentially a lifeline or welfare issue. In order for customers to be able to enjoy the benefits of competition, competitors must be able to price their services based upon their costs as determined by their own efficiencies. Assessment of large subsidies against interexchange carriers will only inflate the price of their services to their customers, which may replicate the private bypass threat caused by the current loading of toll usage charges. Moreover, widespread subsidies reduce the incentive for efficiency to recipient telephone companies. Finally, such non-targeted subsidies flow to all customers regardless of their need, thus diminishing the amount of the benefit available to assist those with a real need.

Thus, local service should not be unnecessarily subsidized. Both USITA and UTS believe that at the end of an appropriate transition period NTS costs should be recovered from end-users, with the exception of those costs subsidized by the FCC's permanent Universal Service Fund. The local loop is a pair of copper wires between the customer's premise and the local telephone company central office, which is exclusively dedicated to an individual customer to receive as well as place both local and long distance calls. A flat-rate charge is appropriate to recover those costs, because they are fixed regardless of the amount of usage of that dedicated facility.

PUBLIC CONCERN

Recent local rate increase requests by large telephone companies (particularly in Texas and California), as well as other filings, have raised genuine concerns among many telephone customers and their representatives. However, we believe that it is important to identify what portion of such requests is due to the proposed implementation of the FCC's Access Charge Plan, and what portions are attributable to the Modified Final Judgment, increased capital recovery (depreciation) needs, and/or higher rate-of-return requirements.

If there were no other pressures on local rates, the net impact of the imposition of access charges on all customers nationwide would be zero. In other words, the increase in a customer's bill due to access charges will be offset by a corresponding reduction in his (or her) long distance charges, on a nationwide average basis. It should be clearly understood that access charges, offset by reduced long-distance usage rates, will not produce increased revenues to local telephone companies.

In that regard, access charges also mean that customers in some states will no longer be called upon to subsidize customers in other states. An example from the United Telephone System illustrates this point. The United Telephone Company of Ohio and the New Jersey Telephone Company both have NTS revenue requirements per access line of about $30.00 per month. Yet, the Ozark Plan (specifically, the Subscriber Plant Factor) allocates different amounts of their respective NTS costs to interstate toll service, largely as result of holding-time and average-length-of-haul (distance) factors. Whereas, the Ohio Company's allocation to the interstate jurisdiction is only $6.00 per access line per month, the New Jersey Company's interstate allocation is $13.00 per access line per month.

DISTORTIONS PRODUCED BY SPF

Company	NTS revenue requirement per access line	NTS costs allocated to interstate toll
UTC of Ohio	$30	$6
New Jersey Telephone	30	13

As you might suspect, local rates in Ohio are significantly higher than in New Jersey. Such distortions, caused by allocations of fixed costs on usage based formulae, cannot be justified in a competitive environment.

The Universal Service Fund contained in the FCC's Access Charge Plan will provide a targeted subsidy to the high cost telephone companies, to protect their customers against extraordinary increases. Indeed, the High Cost Factor proposed by the NARUC/FCC Joint Board (Docket No. 80-286) to fund this substantial subsidy (estimated to total approximately $900 million in 1984), is structured so that no end-user will be assessed an interstate charge for NTS costs more than about 50 percent of the nationwide average accessline costs.

JOINT BOARD HIGH COST FACTOR UNIVERSAL SERVICE FUND

[In percent]

National average NTS costs (percent)	Subscriber access	High cost	Intrastate jurisdiction
0-115	25	0	75
115-160	25	50	25
160-200	25	60	15
200-250	0	95	5
250+	0	100	0

Also, consider that local telephone rates are currently a comparative bargain. In the United Telephone System, residential one-party rates range from a low of $3.65 in the State of New Jersey to a high of $20.25 in Ohio, per month. In that regard, it should also be noted that whereas the Consumer Price Index has increased by 193 percent in the last ten years, the total average price of telephone service has increased by only 63 percent. (See Exhibit No. 4).

In addition, the conversion to access charges means that interstate and intrastate long distance rates could likely decline, from as much as 15 percent to 40 percent over the transition period. Thus, the total telephone bill paid by many customers may not increase as much as feared by some, will be approximately the same for those customers who generally make $20-$30 in long distance calls per month, and should decrease for those customers making more than about $30 in long distance calls per month.

Further, where State regulatory commissions have authorized telephone companies to implement Local Measured Service, customers are given a further opportunity to control the size of their monthly bill.

Finally, the level and structure of the charges for exchange access have a direct effect on uneconomic bypass. There is no single cost of bypass; nor is there a specific price level of exchange access at which bypass will occur. The costs of bypass facilities vary according to the telephone station density of the access area served, the terrain of the area, the loop lengths from the serving node to the customers, the type of technology employed, and economies of scale that are dependent on the level of demand. The demand, in turn, is a function of individual customer usage levels and of the difference in price of bypass service and the price charged for access to the public switched network. Clearly, the FCC's Access Charge Plan allows the maximum flexibility in dealing with the bypass issue by exchange carriers. The transition period will allow each exchange carrier to assess whether their conditions dictate a need for rapid movement toward cost-based pricing. One should keep in mind that some forms of bypass will always be present; i.e. the need for sophisticated communication networks that the public switched network cannot meet, and inhouse communications networks such as large universities and many local and state governments.

Therefore, forbidding all bypass does not seem feasible or practicable to administer. The FCC's Access Charge Plan will send clear price-signals to the marketplace so that (1) companies which have invested heavily in technologies made economic only by the present uneconomic and non-cost based rates will have several years in which to amortize those investments, and (2) the established transition period will encourage investors to target new investments in technologies that are consistent with the underlying costs of the public switched network and, hence, encourage the most efficient possible use of the nationwide telecommunications system.

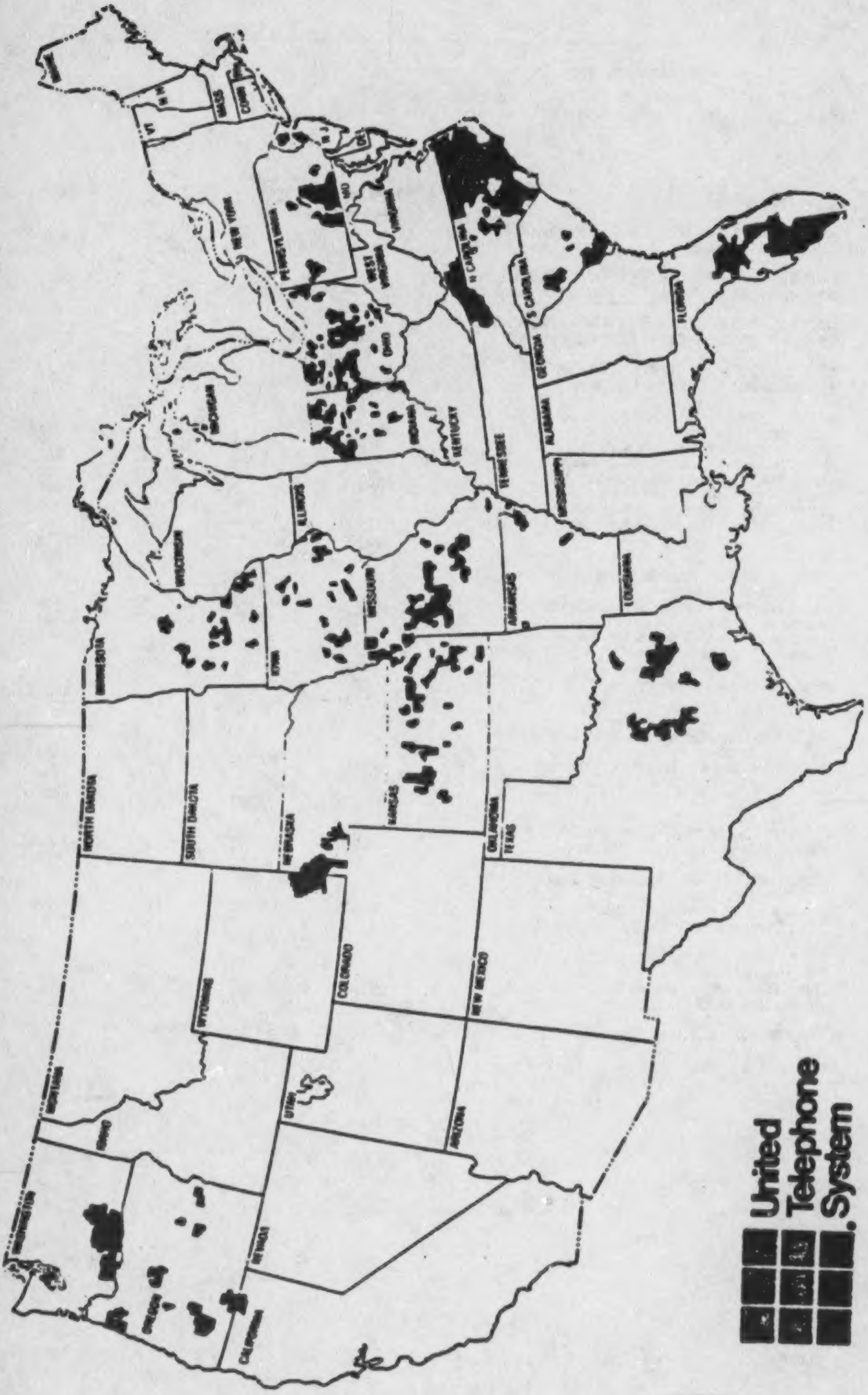
CONCLUSION

For all these reasons, we in the United Telephone System believe that the FCC's Access Charge Plan will work, and that universal service will not be jeopardized. Further, the FCC is developing a post-implementation Access Charge monitoring procedures, to provide early-warning of any threat to universal service, and has provided a waiver procedure to allow for a "lifeline" option to ameliorate the effects of interstate access charges. The FCC is best positioned to timely respond to and resolve (with the State commissions) any rate-related problems. Congress may wish to establish oversight mechanisms to monitor developments and impacts of these FCC actions.

But, we don't believe that federal legislation to alter the FCC's Access Charge Plan is presently needed or appropriate. If, however, the situation should develop that corrective legislation becomes necessary, UTS and USITA will be among the first to seek and support the same.

I very much appreciate this opportunity to share these views and concerns with you. I hope that you will give them serious consideration, because the future viability of the telephone industry and its ability to provide universal service is at stake. Today's telecommunications market is being driven by rapidly accelerating improvements in technology, free market forces and the national trend toward deregulation and competition. In this environment, the prices of all telecommunications products and services are being driven towards their costs. Access charges and other pricing concepts, like LMS, are needed. With you help and understanding, local telephone service can continue to be efficiently provided to the consumers in this country by private industry far into the future, while those same consumers can likewise enjoy all of the benefits of competition in deregulated telecommunications markets.

Thank you very much.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ALABAMA
MISSISSIPPI
ILLINOIS
WISCONSIN
MINNESOTA
IOWA
MISSOURI
ARKANSAS
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TEXAS
MONTANA
WYOMING
COLORADO
NEW MEXICO
IDAHO
UTAH
ARIZONA
WASHINGTON
OREGON
NEVADA
CALIFORNIA

United Telephone System

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United Telecommunications, Inc.

1982 SUBSIDIARY STATISTICS

	Revenues	**Telephone Plant**	**Access Lines**	**Employees**
	(Thousands of Dollars)			
UNITED TELEPHONE SYSTEM, INC.—Westwood, Kansas R.H. Snedaker, President	$ —	$ —	—	646
UNITED TELEPHONE COMPANY OF FLORIDA— Altamonte Springs, Florida, T. W. Todd, President	433,994	1,246,034	606,550	5,314
CAROLINA TELEPHONE AND TELEGRAPH COMPANY— Tarboro, North Carolina, D. W. Peterson, President	340,758	1,014,073	591,592	5,151
UNITED TELEPHONE COMPANY OF OHIO— Mansfield, Ohio, C. G. Fields, President	267,333	730,648	400,558	3,697
MIDWEST GROUP—Overland Park, Kansas R. B. Cashwell, President				
United Telephone Company of Missouri	92,465	247,514	146,182	1,328
United Telephone Company of Minnesota	36,862	112,314	81,983	567
United Telephone Company of Kansas	36,469	102,391	65,227	523
United Telephone Company of Iowa	26,141	82,956	61,793	356
United Telephone Company of the West	16,781	44,499	29,634	194
United Telephone Company of Arkansas	7,510	20,204	15,210	110
	216,228	609,878	400,029	3,078
EASTERN GROUP—Carlisle, Pennsylvania L. G. Wigbels, President				
United Telephone Company of Pennsylvania	118,436	387,883	236,161	1,742
New Jersey Telephone Company	28,275	85,609	37,981	292
United Telephone Company of New Jersey	17,443	48,990	27,511	175
Hillsborough and Montgomery Telephone Company	6,411	18,494	9,430	38
West Jersey Telephone Company	6,288	19,627	9,320	71
Saltillo Telephone Company	823	3,773	2,844	—
	177,676	564,376	323,247	2,318
SOUTHEAST GROUP—Bristol, Tennessee W. W. Hill, President				
United Inter-Mountain Telephone Company	129,474	415,203	223,036	2,147
United Telephone Company of the Carolinas	33,706	107,231	53,468	316
	163,180	522,434	276,504	2,463
UNITED TELEPHONE COMPANY OF INDIANA— Warsaw, Indiana, G. L. White, President	104,269	303,779	158,547	1,304
NORTHWEST GROUP—Hood River, Oregon D. D. King, President				
United Telephone Company of the Northwest Subsidiary: California-Oregon Telephone Co.	65,045	182,781	87,042	696
TEXAS GROUP—Tyler, Texas J. B. Gibson, President				
United Telephone Company of Texas Subsidiary: Palo Pinto Telephone Company	65,141	180,091	91,877	893
TOTAL UNITED TELEPHONE SYSTEM	$1,833,624	$5,354,094	2,935,946	25,560

Exhibit 3

JOINTLY USED, OR COMMON, TELEPHONE FACILITIES

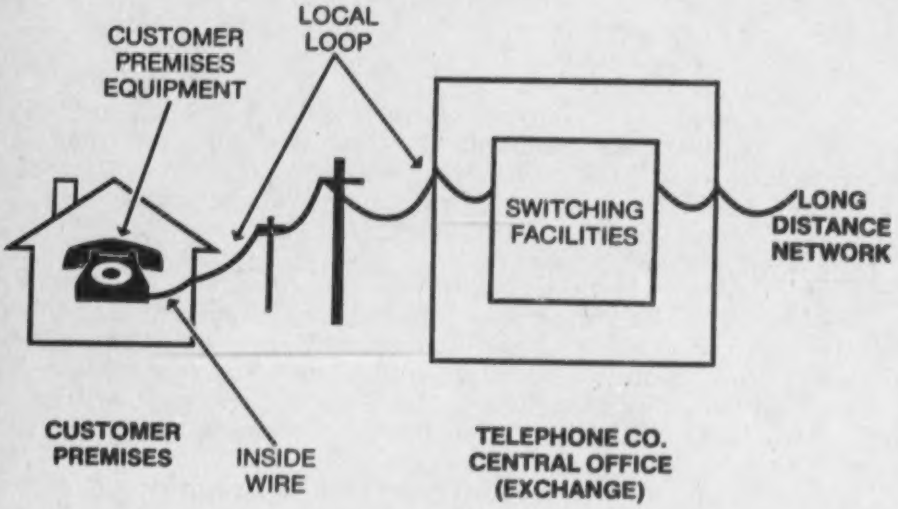
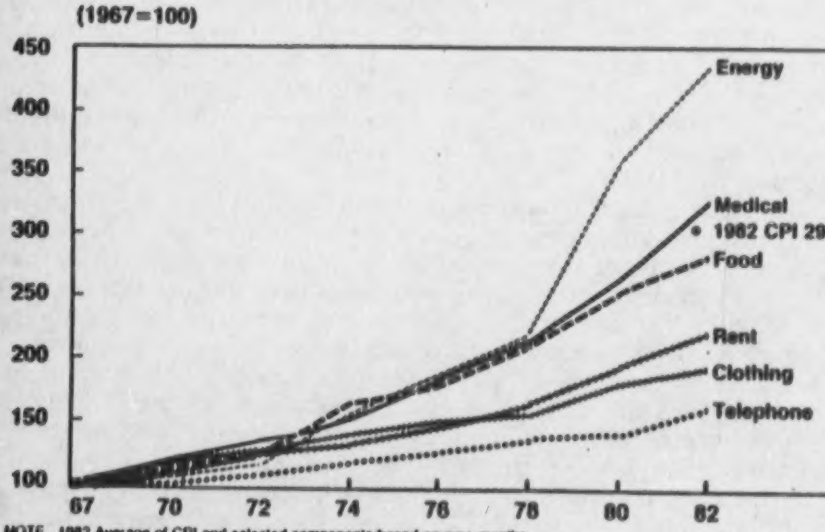

CUSTOMER PREMISES EQUIPMENT
LOCAL LOOP
SWITCHING FACILITIES
LONG DISTANCE NETWORK
CUSTOMER PREMISES
INSIDE WIRE
TELEPHONE CO. CENTRAL OFFICE (EXCHANGE)

Exhibit 4

CONSUMER PRICE INDEX

SELECTED COMPONENTS



NOTE 1982 Average of CPI and selected components based on nine months
SOURCE U.S. Dept. of Labor, Bureau of Statistics U.S. City Average (CPI-U)

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Chairman **Packwood**. Before the next panelist goes on, let me make sure I understand you. You are speaking for the United States Independent Telephone Associations—it is 1,400 companies—and you have no objection to the FCC adding the access charge, which is clearly not going to be just $2; it is going to be apparently $6 or $7 over about 6 years or more. I mean there is no limit to what they can do.

You have no objection to it?

Mr. **Snedaker**. That is correct.

I would like to say that there is not a 100-percent agreement of the 1,432 members, as you probably concluded already, since Mr. Nehring was one of those. But this was the position that USITA took, authorized by its board and executive committee both in docket 78-72 and reconfirmed last Friday.

I speak as first vice president.

Chairman **Packwood**. Mr. Copsey.

Mr. **Copsey**. Good afternoon, Mr. Chairman, members of the Senate Commerce, Science, and Transportation Committee and the House of Representatives Energy and Commerce Committee. We are pleased to testify on behalf of the Rural Telephone Coalition in support of the preservation of universal telephone service in this country.

I am Evan Copsey, president of the Fidelity Telephone Co. of Sullivan, Mo. We serve over 8,400 customer access lines in 80 exchanges. With me are Larry Ware from the Garden Valley Telephone Co. of Erskine, Minn., and Jack Keen of the Western New Mexico Telephone Co. of Silver City, N. Mex.

I request that our respective written statements be made part of the record. We will summarize our positions for the committee.

The rural telephone coalition, the RTC, is composed of three national trade organizations representing the interests of rural telephone companies, the Organization for the Protection and Advancement of Telephone Companies, the National Telephone Cooperative Association, and the National REA Telephone Association. Collectively, these 3 organizations represent over 850 independent telephone companies serving approximately 15 million rural Americans.

Mr. Chairman, the RTC supports the efforts of your committee to preserve univeral telephone service at reasonable rates. For many years, as the industry has moved inexorably towards a fully competitive environment, we have expressed our concern about the impact of the changes in the telephone industry on customers throughout rural America. We are not here today to urge you to turn back the clock. We fully recognize that technological advances, the AT&T divestiture, and the court and the FCC decisions have made clear that the telecommunications industry of tomorrow will exist in a competitive marketplace.

However, our customers in rural America also want to be part of this technological revolution. They, too, should participate in the information age. We are concerned that telephone service may be priced beyond the reach of many Americans if modifications are not made to the recent FCC decisions. As you now move to consider legislation that would preserve universal service and change some of these decisions, we urge you to insure that those in rural America, indeed all Americans, continue to have a high quality telephone service at rates which they can afford. Maintaining universal service at reasonable rates as the industry becomes fully competitive is no easy task. Congress has been struggling with these competing goals for over 7 years. The issues are clearly focused. The solutions are at hand. We cannot afford to wait and see how many people are left without telephone service.

The RTC believes that Congress can and must act now. We believe the legislation should address the following principles:

First, end-users should not pay directly for subscriber line costs allocated to toll.

Second, a universal service fund to deal adequately with telephone service in high cost areas must be developed.

Third, all providers of telecommunications services, including bypassers of local facilities, should contribute equitably to the costs of providing local telephone service.

Fourth, the deaveraging of toll rates should be prevented.

Fifth, consistent and uniform regulatory policies between Federal and State jurisdictions should be implemented.

Now I would like to turn over to Larry Ware for his further statements of the RTC.

[The statement follows:]

Statement of Evan Copsey, Fidelity Telephone Co., on Behalf of the Organization for the Protection and Advancement of Small Telephone Companies (OPASTCO)

Mr. Chairman, members of the Senate Commerce, Science and Transportation Committee and the House of Representatives Energy and Commerce Committee, I am pleased to offer this testimony on behalf of Fidelity Telephone Company and the Organization for the Protection and Advancement of Small Telephone Companies (OPASTCO) on the subject of today's hearing, the preservation of universal telephone service in this country.

I am the President of Fidelity Telephone Company of Sullivan, Missouri. We serve 8,364 customer access lines in eight exchanges. OPASTCO is a trade association representing over 350 rural telephone companies and cooperatives in 42 states, most of whom serve fewer than 25,000 access lines. Collectively, we serve nearly 2 million customers.

Mr. Chairman, OPASTCO fully supports the efforts of your committees to preserve universal telephone service at reasonable rates for our customers. For many years, as the industry has moved inexorably towards a fully competitive environment, we have expressed our concern about the impact of the changes in the telephone industry on our subscribers in rural America. The goals of preserving universal telephone service and moving towards a competitive telecommunications industry are often in conflict. Only Congress can resolve these issues and enact sufficient protections to assure continued availability of telephone service. We are not here today to urge you to turn back the clock. We fully recognize that technological advances, the AT&T divestiture, and FCC and court decisions have made clear that the telecommunications industry of tomorrow will exist in the competitive marketplace and will not be characterized by monopoly provision of any services.

However, Mr. Chairman, our customers in rural America also want to be part of this technological revolution. We, too, want to participate in the Information Age. We are concerned that telephone service may be priced beyond the reach of many of our subscribers if modifications are not made to recent FCC decisions. As you now move to consider legislation that would preserve universal service and change some of these decisions, we urge you to ensure that those in rural America, indeed all Americans, continue to have high quality telephone service at rates which are affordable.

Maintaining universal service at reasonable rates as the industry becomes fully competitive is no easy task. Congress has been struggling with these competing goals for over seven years. OPASTCO believes that Congress can and must act now. The issues are clearly focused, the solutions are at hand. We cannot afford to wait and see how many subscribers are left without telephone service when we have the ability to prevent such a consequence now.

OPASTCO believes that legislation to preserve universal telephone service should address the following principles: (1) all providers of telecommunications services, including bypassers of local facilities, should contribute equitably to the costs of providing local telephone service; (2) a Universal Service Fund to deal adequately with telephone service in high cost areas must be developed; (3) consistent and uniform regulatory policies between federal and state jurisdictions should be implemented; (4) end users should not pay directly for the costs of the local telephone lines; and (5) toll connecting links whose costs are significantly higher than the national average should be compensated for by the Universal Service Fund.

I. ALL TELECOMMUNICATIONS PROVIDERS SHOULD CONTRIBUTE EQUITABLY TO THE COSTS OF UNIVERSAL TELEPHONE SERVICE

Mr. Chairman, OPASTCO believes that all providers of telecommunications services should contribute fairly to the costs of providing universal service. Providers of telecommunications services which bypass the local distribution facilities of exchange carriers should also share the cost of these local facilities. Although competition has increased and alternative technologies have been developed, we have not seen a stampede of carriers wishing to serve high cost rural areas or residential subscribers. Competitors have naturally entered markets which are profitable and have not chosen to serve the high cost and lower density markets. Yet all telecommunications service providers benefit from the universality of telephone service, all providers benefit from using existing facilities as a back-up or to expand their own networks. Thus their profitability is increased by universally available telephone service. We believe they should all contribute to the cost of preserving these universal local facilities.

II. UNIVERSAL SERVICE FUND

Legislation should ensure that a Universal Service Fund (USF) is created that will adequately protect exchange carriers that serve high cost areas. We believe that exchange carriers whose costs exceed the national average by more than 110 percent should be eligible to receive funds from the USF. We also believe that these eligible carriers should recover all of their costs from the USF which exceed the national average in order to ensure that they are able to continue providing service in high cost areas and that their customers are able to afford telephone service.

III. CONSISTENCY AND UNIFORMITY OF FEDERAL AND STATE REGULATORY POLICIES

In recent years, as competition in telecommunications has been sanctioned by the federal courts and the FCC, there has been increasing conflict between the federal and state regulatory bodies. OPASTCO believes that consistent regulatory policy is essential to the continued financial viability of our telephone companies. As Congress acts to set out clear goals for national telecommunications policy, it should act to ensure consistent regulatory policy at the federal and state level. As telephone companies try to provide high quality service to our customers and take advantage of new technology to reduce costs. we are the ones that suffer from the constant confrontations between federal and state regulatory policies. We believe that Congress can eliminate these needless and costly regulatory battles by setting clear national policy direction. The economic health of our companies and thus our ability to serve our customers depend on it.

IV. END USERS SHOULD NOT PAY DIRECTLY FOR THE COSTS OF SUBSCRIBER LINES

As you are all aware, the FCC's Decision in Docket 78-72 would transfer, over a transitional period, most costs of the customer's access line to the interstate telephone network directly to subscribers or end users at a flat rate. This would be true whether or not these customers ever made a long distance call. The essential rationale for the FCC's Decision was to prevent the uneconomic bypass of local facilities by heavy users of telecommunications services who pay a disproportionate share of the fixed cost of local facilities through usage based rates. We believe the Commission went too far. By attempting to cure one problem, they have created another. The transfer of all of these fixed costs to end users places an excessive burden on residential customers, particularly in high cost rural areas. If these costs are charged directly to our customers, many will simply not be able to continue to have basic telephone service. Furthermore, if end users must pay all local loop costs on a flat rate basis, there is no incentive for exchange carriers to make investments in new modern facilities. Interexchange carriers depend on these facilities and benefit from continued upgrade and introduction of new technology. We urge Congress to change this portion of the FCC Decision and modify end user charges.

V. HIGH COST TOLL CONNECTING LINKS SHOULD BE SUPPORTED BY THE UNIVERSAL SERVICE FUND

In low density rural areas, the costs of providing service between the local telephone company central office and the toll network are exceedingly high. These toll connecting links or Class 4 to Class 5 links, as they are often called, constitute the part of the telephone network where there is the greatest variance in cost. If exchange carriers are forced to charge interexchange carriers directly for the costs of these toll connecting links, the pressure to deaverage toll rates for calls in and out of rural areas will be severe. OPASTCO believes that the Unversal Service Fund should provide a contribution to the cost of these high cost toll connecting links in order to prevent excessively high toll rates for rural areas.

VI. SUMMARY

In summary, Mr. Chairman, OPASTCO believes that Congress must act now to preserve universal telephone service. We believe that any legislation which is enacted should include the following points:

1. All providers of telecommunications services should contribute to the cost of providing universal telephone service.
2. An adequate Universal Service Fund should be developed. Exchange carriers whose costs exceed 110 percent of the national average should recover all costs from the USF.
3. Uniform and consistent federal and state regulatory policy should be implemented.
4. End users should not pay directly for the costs of customer lines.
5. High cost toll connecting links should receive a contribution from the USF.

We look forward to working with you to enact this needed legislation.

Chairman **Packwood**. Mr. Ware.

Mr. **Ware**. Thank you, Mr. Chairman.

I am Lawrence Ware, manager of the Garden Valley Telephone Co. of Erskine, Minn. We serve 12,000 subscribers in northwestern Minnesota, and it is a telephone cooperative.

As Evan said, I would like to expand on some of the principles he cited. The first is the end user should not pay directly for subscriber line costs allocated to toll. As you are all aware, the FCC's decision in docket 78–72 would transfer over a transitional period most costs of the consumer's access line to the interstate telephone network, directly to subscribers or end users at a flat rate. This would be true whether or not these customers ever made a long distance call.

The essential rationale for the FCC's decision was to prevent the uneconomic bypass of local facilities by heavy users of telecommunications services. We believe the commission went too far. By attempting to cure one problem, they have created another. The transfer of all of these fixed costs to end users places an excessive burden on rural or residential customers, particularly in high cost areas. If these costs are charged directly to our customers, many will simply not be able to continue to have basic telephone service.

We urge Congress to eliminate end user charges.

Second, the universal service fund. Legislation should insure that a universal service fund is created that will adequately protect exchange customers in high cost areas. We believe that exchange carriers whose costs exceed the national average by more than 110 percent should be eligible to receive funds from the universal service fund. We also believe that these eligible carriers should recover all of their costs from the universal service fund which exceed 110 percent of the national average in order to ensure that they are able to continue providing service in high cost areas, and that their customers are able to afford telephone service.

Third, all telecommunications providers should contribute equitably to the costs of universal telephone service.

Mr. Chairman, the Rural Telephone Coalition believes that all providers of telecommunications services should contribute fairly to the costs of providing universal service. Providers of telecommunications services which bypass the local distribution facilities of exchange carriers should also share the cost of these local facilities. Although competition has increased and alternative technologies have been developed, we have not seen a stampede of carriers wishing to serve high cost rural areas or residential subscribers. Competitors have naturally entered markets which are profitable and have not chosen to serve the higher cost and lower density markets. Yet all telecommunications service providers benefit from the universality of telephone service. All providers benefit from using existing facilities as a backup or to expand their own networks.

Thus, their profitability is increased by universally available telephone service. We believe they should all contribute to the cost of preserving these universal local facilities.

Now I would like to turn the microphone over to Mr. Keen who would conclude our statement.

[The statement follows:]

STATEMENT OF LAWRENCE C. WARE, GARDEN VALLEY TELEPHONE CO., ERSKINE, MINN., ON BEHALF OF NATIONAL TELEPHONE COOPERATIVE ASSOCIATION

Good Morning, Mr. Chairman and Members of the Subcommittee. My name is Lawrence Ware, and I am the Manager of the Garden Valley Telephone Company in Erskine, Minnesota. Today, I also represent the National Telephone Cooperative Association, NTCA.

NTCA is a national trade association comprised of approximately 400 locally owned and operated small telephone systems providing service in rural areas in more than 40 states. Most of these systems have obtained capital financing under the loan programs of the Rural Electrification Administration (REA).

Garden Valley Telephone Company is a subscriber-owned cooperative providing telephone service to about 12,000 customers in rural Northern Minnesota.

NTCA is a member of the Rural Telephone Coalition. The Rural Telephone Coalition (RTC) is comprised of the three national trade associations representing the interests of rural telephone companies: the Organization for the Protection and Advancement of Small Telephone Companies, the National Telephone Cooperative Association and the National REA Telephone Association. The Coalition was formed in 1979 to defend and advance the rights and interests of rural telephone subscribers during the Congressional and regulatory agency debates on national telecommunications policy reform. Collectively, these three organizations represent over 850 independent telephone companies, serving approximately 15 million rural Americans throughout rural America.

I appreciate the opportunity to appear before you today to testify. I support the effort of the chairman and Committee members to preserve universal telephone service. As the manager of a small independent telephone system, I am well aware that we will need this kind of support if small telephone systems are to survive and the rural consumer reap the benefits of improved telecommunications under the new access charge system that the FCC has designed.

We have developed the best telephone system in the world because of the congressionally mandated goal of universal telephone service. The goal is stated in the Communications Act: "to make available, so far as possible, to all the people of the United States a rapid, efficient, Nationwide, and world-wide wire and radio communication service with adequate facilities at reasonable charges. . . ." This mandate was clearly interpreted by the FCC in its access charge decision *Third Report &*

Order. The Commission stated, "We have concluded that the 'available . . . to all' language does contemplate that telephone exchange service should be made available at reasonable rates."[1] However, I believe the public policy goal of universal service at reasonable rates has been shaken by the Commission's Access Charge decision.

Today, I would like to focus on the impact of the FCC decision on Garden Valley and other small companies. Much of the available data comes from estimates compiled by the Rural Electrification Administration, or REA.

As a rule, the over 940 REA borrowers provide service to rural, high-cost areas. Since serving sparsely-settled areas requires more plant (cable, poles, etc.) to serve each subscriber, REA borrowers typically must invest much more on a per subscriber basis than does the Bell system. REA borrowers have invested an average of $1,836.36 per subscriber. For Garden Valley the amount is $2,022.22 per subscriber. Many rural telephone systems have as much as 90 percent of their investment in non-traffic sensitive (NTS) plant, while the average Bell Company, as of 1981, had about 50 percent.

REA borrowers have an average of 5.43 subscribers per route mile of line (1981 statistics) while Garden Valley has 2.91 subscribers per route mile. REA borrowers have an average local area calling scope of about 2,000 people. Garden Valley has many subscribers who can reach only 500 to 600 others, while half reach about 1,300 on a local call. Most urban local calling scope reaches hundreds of thousands and even millions.

Today, a significant portion of the expense of local facilities which are used by both long distance and local services is allocated to and considered a cost of long-distance service. Traditionally, these costs have been recovered from a pool of interstate long distance revenues. The costs of these local facilities are allocated between long distance and local service on the basis of a formula found in the NARUC-FCC "Separations Manual."

NTCA recognizes that there is a need to revise the present system of compensation of local exchange carriers for origination and termination of intercity traffic. The present system of settlements contracts and the ENFIA traiffs for OCCs are filled with inconsistencies which create constant conflict.

FCC ACCESS CHARGE DECISION

In its access charge decision, the FCC recognized the problems of high cost telephone systems. The FCC affirmed its congressionally mandated goal of universal telephone service, and admitted this goal would be jeopardized if subscriber were forced to pay high access charges. Therefore, the FCC included in its access charge plan a Universal Service Fund (USF) to be used to assist high cost local companies in keeping access charges reasonable. The Federal/State Joint Board was directed to recommend the details of the USF.

The impact of the access charge plan depends in large part on how the USF is implemented. In April, 1983, the Joint Board agreed to recommend a formula for designating those NTS costs which were eligible for recovery from the USF. While the Joint Board recommendation has not yet been issued in textual form, the terms stated in Joint Board press statements provide for eligible costs to be limited to those above 115 percent of the national average of such costs. Only a percentage of those costs above 115 percent can be recovered from the USF. Under the Joint Board proposal, interstate access charges in rural areas would still be allowed to rise to as high as 156 percent of the national average charge. In addition, the Joint Board has proposed that the calculation of the high cost factor be based on the cost of debt of the individual company. This proposal would penalize rural companies who borrow from REA and would increase the eligibility of large companies. The USF is to be phased in over three years, beginning in 1986.

CRITIQUE OF FCC DECISION

In arriving at its decision, the FCC attempted to balance the conflicting concerns of subscriber drop-off due to high access charges and the loss of high volume users through bypass. However, the FCC decision does not contain quantitative analyses sufficient to justify its premises.

The FCC based its decision on the hypothesis that the demand for local service, including access charges, was relatively inelastic. However, in reaching this conclusion, the FCC used a very limited record. Studies available and in the FCC record, however, indicate that a substantial drop-off of local subscribers could result from high access charges, particularly where combined with similarly determined intrastate access charges. Furthermore, the access charge decision was reached before the Joint Board has recommended a high cost factor.

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[1] MTS/WATS Market Structure, CC Docket 78-72, *Third Report & Order*, December 22, 1982, p. 28. (hereinafter *Third Report & Order*).

In particular, the FCC itself referred to a study performed by Dr. Lewis J. Perl of NERA [2] which AT&T had introduced in its antitrust trial. It indicated significant elasticity of demand for telephone service, especially among rural poor. The Perl study found that a 100 percent increase in basic telephone rates would result in a drop-off of subscribers to 83.69 percent and a 200 percent rate increase would lead to a 70.92 percent subscriber level. Whereas Perl concluded that 888.84 percent of rural persons currently had telephone service, with 100 percent rate increases, this percentage declined to 79.10 percent.[3] For moderately poor rural persons, a 100 percent increase in the price of telephone services resulted in a decline to 64.50 percent.

It should be noted that Appendix G of the Commission's access charge decision [4] includes another paper by the National Economic Research Associates, Inc., that was not subjected to public comment. This paper purports to recalculate the impacts of the access charge plan described in the Perl study, using increases of $2 and $7 on the assumption that these charges were in the range contemplated by the Commission. This assumption is invalid for two reasons. First, the $7 price is based on the Bell national average non-traffic sensitive per subscriber line cost. The Commission's order, however, effectively eliminated national averaging except for a then-undetermined high cost factor. Rather than Bell nationwide averages, the relevant range of costs, and hence prices, was shown to be up to $27 for individual companies and much higher for some independents. Second, the $7 figure is misleading because it does not reflect the fact that the states are urged to adopt the same formula on *intrastate* access charges. Therefore, even the average figure must be at least doubled if the effect on the consumer is to be measured.

It is therefore apparent that the Commission had good reason to believe that rather than demand for service being inelastic, a decrease of almost 8 percentage points in national telephone penetration, or approximately 7 million households (assuming 80 million residential subscribers) could be expected.

Some cases which have received public attention suggest a strong correlation between telephone rate increases and subscriber drop-off. While other factors may be operative in these cases, they deserve examination as an indication of subscriber reaction to increases of a magnitude anticipated under the FCC access charge plan. One such case is that of Hickory Telephone Company, described in testimony presented before the House Telecommunications Subcommittee on March 22, 1983. Hickory raised its local rates in 1975 from $10.66 to $16.35, a 54-percent increase. Consequently, 14 percent of the customers discontinued their basic telephone service.[5] In another case, the Big Run Telephone Company in Pennsylvania requested and received approval for a substantial local rate increase to cover the costs of purchasing some used switching equipment. Approved in April, 1981, the new rate was an increase of about 40 percent, to a total of $21.75. Within several months, 22 percent, or 204 of the system's 924 subscribers dropped service. Although some have reconnected since that time, as of the end of 1982, most had not.

Several studies have been performed in an effort to quantify the impact of access charges on rural telephone rates. I have attached as Appendix II [6] a preliminary survey of the impact on Minnesota independent telephone systems of the recent FCC and Joint Board decisions. This survey includes estimates of the interstate access charges and the full price of continued access to the telephone network which subscribers of these systems will pay if the state patterns its new cost recovery system on the FCC model.

According to the survey, interstate access charges will range from $4.70 to $21.48 per subscriber line per month. Garden Valley's customers will pay interstate access charges of $6.31. Intrastate access charges will range from $4.43 to $20.94; Garden

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[2] "Economic and Demographic Determinants of Residential Demand for Basic Telephone Service," Dr. Lewis J. Perl of National Economic Research Associates, Inc., for FCC Docket No. 20003, on behalf of AT&T. Presented in AT&T/DOJ Antitrust case as Defendant's Exhibit D-4-518. Table attached as Appendix I.

[3] Appendix I.

[4] *Third Report* and *Order*, Supra note 1, at appendix G.

[5] Testimony of Michigan Public Service Commission, Chairman Eric J. Schneidewind before the House Subcommittee on Telecommunication, Consumer Protection and Finance of the Energy and Commerce Committee, March 22, 1983.

[6] Appendices II–V were not reproducible and have been retained in the committee files.

Valley's will be $8.90. Implementing the FCC's High Cost Factor will benefit only eight companies, with the highest cost companies receiving $11.83 per subscriber line per month and the lowest eligible company receiving only 50¢ per subscriber line per month. Most Minnesota independent companies including Garden Valley, will receive virtually nothing.

A study by REA (Attached as Appendix III.) was based on a posttransition era, and assumed deregulation of CPE and inside wiring, as well as on the High Cost Factor (CC Docket 80-286) as announced in the Joint Board's press release of April 16, 1983. According to the REA study, 650 REA borrowers would have average monthly subscriber rates, including projected interstate and intrastate access charges, 100 percent or more increased over the 1981 local rate. For over two-thirds of REA borrowers, interstate access charges will be least double local rates.

Another example of the impact of the access charge and Joint Board decisions is provided by Golden West Telecommunications Cooperative, Inc. (Appendix IV). The cooperative serves 5,531 subscribers in Western South Dakota. If the FCC plan is implemented for both interstate and intrastate access, Golden West will have increased local rates from $5.80 to $22.50, a 288 percent increase. It would have a combined interstate and intrastate rate of $16.76. In rural areas where distances to schools and hospitals are great, more intrastate toll calls are made, so the increase would be considerable.

Finally, I would like to share with you the study done of the projected access charges and rate increases among the members of the Texas Statewide Telephone Cooperative, Inc. (Texas Statewide) (Appendix V). This study also includes estimates of access charges for intrastate service which would result from implementation of an FCC-type plan by the Texas Public Utility Commission.

The average basic monthly rate among these systems is $8.77. The number of subscribers they reach ranges from a few hundred to a few thousand. The interstate access charges as proposed by the FCC will range from $4.20 to $7.08 with an average high cost factor of $6.82. Intrastate access charges, if patterned after the FCC plan, would range from $6.72 to $21.47 and the total monthly rate at the end of the transition period would be increased from 83 percent to 488 percent, with the average of 193 percent.

Some access charges would be considerably more than would be others. Of the 21 companies studied, 14 would have monthly rates over $25 and 8 over $30.

In light the Perl findings, it is clear that the implementation of the FCC access charge decision will have a serious impact on universal service in rural areas.

Another premise of the FCC access charge decision is that implementing end user charges would reduce bypass. In the text of the decision, the Commission staff listed various instances of bypass.

However, the staff failed to analyze whether such bypass would be reduced by any significant degree by the FCC decision. The FCC provided no quantitative analyses to demonstrate that it had considered the benefit of the public as a whole. For all that the FCC knows, the amount of customer rate increases avoided as a result of bypass deferred may be significantly less than the increases its plan will unquestionably impose.

NTCA POSITION

NTCA believes that there are several issues which need to be addressed in legislation to preserve universal service at reasonable rates.

I. Preservation of universal service at reasonable rates

Although the FCC has faithfully recited its intentions to preserve universal service, it is my belief that it has thrown the balance too far in favor of the interexchange carriers and large users at the expense of local subscribers. In some cases this will be merely inequitable; in others it will seriously endanger universal service.

The High Cost Factor appears to be inadequate to protect universal telephone service, especially since State public service commissions are under enormous pressure, both practical and political, to implement similar access charges for intrastate service. In many high cost areas, these intrastate charges will be substantially greater than the FCC charges.

Several bills have been introduced in an effort to address these problems. The bills adopt a variety of mechanisms intended to protect universal telephone service.

A. Eliminate the end user charge.—NTCA supports the elimination of the end user access charge and supports the continuation of a carriers' charge in a manner that is fair and reasonable for all. It makes more sense for interexchange carriers to be charged the access fee. Through control of their pricing strategies they have the flexibility to distribute the costs among their users. Local exchange origination and termination functions are essential to the operations of interexchange carriers and are not otherwise available on a universal basis. It is the interexchange carrier which requires the use of the exchange carriers' facilities and not the other way around. Therefore, at a minimum, the costs of the local facilities should be shared between those who use them, including interexchange carriers.

National Universal Service policies and the REA policy of area coverage have encouraged extending service without regard to individual subscriber line costs. Some of these costs should be paid by the interexchange carrier.

B. Adopt a high cost factor.—Some measures propose a Universal Service Fund for the recovery of NTS costs. If adopted, such a mechanism should allow recovery of 100 percent of the costs over 110 percent of the national average. Such a formula was in S. 898, the telecommunications bill which passed the Senate in 1981 and in H.R. 5158 which passed out of the house Subcommittee on Telecommunications in 1982. Furthermore, NTCA recommends that the Congress repudiate the recommendation of the Joint Board that the individual company's actual cost of debt be used in its cost calculation. This requirement penalizes those telephone systems that borrow from the programs of the REA because it lowers their costs relative to those of non-REA borrowers. National average NTS costs are calculated using a national average cost of debt; for consistency the national average cost of debt should also be used to calculate the high cost factor.

II. Protection of local telephone companies from bypass

Any system adopted to protect local ratepayers should provide for contribution to the support of universal telephone service by telecommunications services that allow big-volume business customers to bypass local facilities. Many such services connect to the public network on the receiving end. Even totally private systems rely on the public network for back-up.

In many cases, the local telephone company has already constructed facilities to serve the large user. When such a user decides to leave the network for a competitive carrier, the remaining local subscribers must then pay for facilities and capacity built to accommodate the large user.

State and Federal regulators should have at their disposal the tools to regulate alternative technologies as they do telephone systems, if it is necessary to do so to maintain universal telephone service.

III. Maintain nationwide toll rate averaging

All low-density toll routes, such as those in rural areas, benefit from our current national policy of toll rate averaging. Toll rate averaging is a pricing concept whereby a customer pays equally for interstate calls across equal distances, time of day and duration. However, it is not clear whether this policy will be continued. We believe that there may be several approaches to continuing toll rate averaging.

Specifically, we believe that legislation should address the higher cost of rural class four to class five toll connecting links.[6] An REA study of Local Service Rates and Toll Bills for Subscribers in Rural Areas shows that the rural toll link costs seven times as much as an equivalent urban toll route.[7] These costs were considered part of the traffic sensitive elements in the FCC access charge decision and charged to interexchange carriers. These higher costs should be included in the nationwide toll support mechanism or in some pooling arrangement. Otherwise their higher costs may discourage alternative interexchange carriers from serving rural areas or will encourage toll rate deaveraging in service from high cost to high cost areas. As stated above, rural users throughout the country have local calling areas with fewer telephones to reach than urban users. Consequently, rural users are more dependent on long distance service to reach essential services such as doctors, hospitals, schools, etc. NTCA urges Congress to include in universal service legislation an explicit statement of support for continued averaging of toll rates nationwide. If legislation is adopted to provide for carrier access charges, provisions should be made to protect deaveraging of toll rates in high cost areas.

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[6] Deaveraging of Interexchange Toll Rates Due to the Introduction of Competition—Preliminary Estimates, National Telecommunications and Information Administration, 1979.

[7] REA Study of Local Service Rates and Toll Bills for Subscribers in Rural Areas, Appendix to Comments of the Rural Electrification Administration in Docket 78-72, March 1980.

IV. Minimize regulation of small telephone companies

Under Section 2(b)(2) of Title II of the Communications Act, small exchange telephone companies, as intrastate carriers, are exempt from many of the FCC regulations and reporting requirements. Unless carefully designed, new mechanisms for recovering local costs may impose heavy new reporting and filing requirements on small companies. NTCA also supports the policy of equal interconnection. However, we urge that economically infeasible requirements for such interconnection not be imposed on small companies with electro-mechanical or older switches. At a minimum, implementation schedules should recognize the technical and financial constraints of small companies and allow flexibility in meeting these standards. NTCA urges Congress in considering common carrier legislation to continue the Section 2(b)(2) exemption for small local telephone companies.

CONCLUSION

The ramifications of the FCC access charge decision are wide-ranging. If interstate and intrastate access fees increase by over 100 percent, as they will in high cost areas, a significant portion of subscribers will drop off the network. This will be detrimental to all users of the network.

The question that these Committees and eventually the Congress must ask themselves is how many people will disconnect from the telephone service because of the rate increases before we have an end to universal service? Since agriculture is one of the linchpins of our economy as well as our foreign trade, how much will rural telephone service and the nation be injured by the economic price experiment of shifting costs from the big businesses and other heavy toll users to the average residential American? How will higher telephone rates effect the continued development of the infrastructure of rural America? Those who drop off the network will not have rapid access to police, fire, and medical service. Businesses will not be able to contact their employees immediately. The rural and urban poor will be isolated without adequate transportation or communications. Is the benefit worth the risk? Is the public interest being served by the FCC access charge system? We in rural America do not believe it is, and share the concern with residential customers.

We appreciate your concern, Mr. Chairman and all the members of the Committees for your interest in preserving universal telephone service at reasonable rates. We look forward to working with you to preserve affordable telephone service. Thank your for this opportunity to testify.

APPENDIX I.—ESTIMATED PERCENTAGE OF HOUSEHOLDS WITH BASIC TELEPHONE SERVICE [1]

Demographic characteristics	Price increase			
	Base	50 percent	100 percent	200 percent
All	91.52	88.15	83.69	70.92
Young	85.39	80.12	73.54	56.92
Black	86.37	81.38	75.08	58.89
Rural	88.84	84.59	79.10	64.28
Moderately poor	83.81	78.12	71.11	53.93
Young	72.18	64.14	55.22	36.97
Black	75.25	67.71	59.12	40.74
Rural	79.26	72.48	64.50	46.34
Very poor	79.28	72.52	64.53	46.38
Young	64.99	56.14	46.88	29.56
Black	69.21	60.78	51.66	33.69
Rural	73.85	66.07	57.31	38.96

Source: Household demographic and economic data: U.S. Department of Commerce, Bureau of the Census. "Money Income of Households in the United States: 1979" (Washington, D.C., U.S. Government Printing Office). U.S. Department of Commerce, Bureau of the Census, "Household and Family Characterisitics: March 1980" (Washington, D.C., U.S. Government Printing Office). Telephone rate information: American Telephone & Telegraph Co., Market and Service Plans Department, Research Section, Market Research Information Systems (MRIS).

Mr. **KEEN**. Mr. Chairman, my name is Jack Keen. I am president of the Western New Mexico Telephone Co. I live in Silver City, N. Mex.

We have an independent company out there. We serve 1,901 subscribers. We have 7 exchanges, none of them over 400 or 500 lines.

We cover a 10,000-square-mile area, and that is about the size of the State of Maryland. And Maryland has 1,433 times more telephones as my company. We have about 1.1 subscribers per mile, and it is all up in the mountains.

The two points I was going to cover, the first one is total deaveraging should be prevented. The RTC believes that nationwide average toll rates have benefited all Americans, particularly those in high-cost rural areas. We are afraid that the transition toward full competition and interexchange services will create irresistable pressures to deaverage toll rates.

For example, in low density rural areas, the costs of providing service between the local telephone company's central office and the toll network are exceedingly high. If exchange carriers are forced to charge interexchange carriers directly for the cost of these links, the pressure to deaverage toll rates for calls in and out of rural areas will be severe.

The RTC believes that the universal service fund should provide a contribution to prevent excessively high toll rates for rural areas.

And then our last point is consistency and uniformity of Federal and State regulatory policies. In recent years, as competition in telecommunications has been sanctioned by the Federal courts and the FCC, there has been increasing conflict between the Federal and State regulatory bodies. The RTC believes that consistent regulatory policies is essential to the continued financial viability of our telephone companies. As telephone companies try to provide high quality service to our customers and take advantage of new technology to reduce costs, we are the ones that suffer from the constant confrontation between Federal and State regulatory policy.

The interests of the telephone industry and American consumers are best served when State and Federal regulatory actions are not in conflict.

Now, in summary, Mr. Chairman, the RTC believes that Congress must act now to preserve universal telephone service. We believe that any legislation which is enacted should include the following points:

End-users should not pay directly for subscriber line costs allocated to toll.

An adequate universal service fund should be developed. Exchange carriers whose costs exceed 110 percent of the national average should recover all costs from the USF.

All providers of telecommunications services should contribute to the cost of providing universal telephone service.

Toll deaveraging should be prevented.

Uniform and consistent Federal and State regulatory policies should be implemented.

We look forward to working, too, with the Congress to enact this legislation, and we would attempt to answer any questions you might have.

[The statement follows:]

STATEMENT OF JACK C. KEEN, PRESIDENT, WESTERN NEW MEXICO TELEPHONE CO., SILVER CITY, N. MEX., ON BEHALF OF NATIONAL REA TELEPHONE ASSOCIATION

Mr. Chairman and members of both Committees, good morning.

My name is Jack Keen. I am President of the Western New Mexico Telephone Company in Silver City, New Mexico, an independent telephone company that serves 1,901 subscribers from seven rural exchanges in Southwestern New Mexico. My subscribers are scattered over a 10,000 squre mile area, an area about the size of the State of Maryland. But Maryland has 1,433 times as many telephones as my company. We have about 1.1 subscribers per route mile.

I am here on behalf of the National REA Telephone Association, usually known as NREATA. NREATA is a national trade association that represents approximately 350 telephone companies that are borrowers under Rural Electrification Administration (REA) programs. NREATA is one of the three organizations that make up the Rural Telephone Coalition.

My reason for being here today, like yours, is to talk about how to keep telephone service affordable for Americans. I know you are concerned about the proposals to raise local rates in your states and districts. We are worried about the rates we will have to charge the customers we serve if something is not done soon. I want to start by emphasizing how much the Rural Telephone Coalition appreciates your interest in this problem and the cooperative effort by both houses of Congress to solve it.

The threat of unacceptably high rates for telephone customers is a result of the explosive growth of technology in recent years and fundamental changes in telecommunications policy. The new national communications policy looks more and more to competition rather than regulation to determine the services that will be available and the prices that customers will pay for them. It is certainly not my purpose in testifying to object to these policies.

I believe that competition and technological advances can be fostered in this country without abandoning the long-standing policy of fostering affordable telephone service for Americans throughout the country. But I believe that a fair method for making all users of the national network share it supporting it is necessary to harmonize these competing goals. The problem as I see it is with the way the Federal Communications Commission has gone about trying to reach these goals. The FCC has taken a piecemeal approach to changing the structure of the communications marketplace. It let the genie of competition out of the lamp. But it lost control of the marketplace forces it set out to foster. The result is that it has not adequately protected the average American customer. Indeed, the FCC probably cannot keep rates reasonable now. Let me explain what I mean by this by talking about the problem in rural areas, since our areas are good examples of the problem at its worst.

For many years, it has been national policy to extend basic telephone service to as many people as possible. When there was no competition, it was easy to implement this policy by treating the nationwide network as an integrated system. The Bell System and independent companies functioned together as a "partnership" to offer long distance service throughout the nation. Rates were averaged so that residents of high cost areas could obtain service at rates based on system-wide costs. Separations procedures also helped to support affordable local rates in high cost areas by allocating substantial costs to toll service. The competitive marketplace would not have accomplished this on its own. In fact, many rural companies would not have been built at all if it were not for the REA loan program that provides financing for construction. The REA programs do not provide operating funds. However, the costs of providing service are at their highest in low density rural parts of the country.

As I mentioned before, my company has only 1.1 subscribers per route mile. Also, in my company the total investment per customer (using 1983 costs) is $11,139. Owing to these high unit costs, the support from rate averaging and separations procedures has been particularly important in rural areas like the one I serve.

With averaged rates, my customers pay long distance rates comparable to what other subscribers in the country pay. Moreover, my company's local rates are affordable mainly because in the past, more than 90% of all revenues have come from toll settlements, and much of that has come from interstate MTS and WATS settlements.

The introduction of long distance competition has created very strong pressures to decrease the contribution that toll service makes to nontraffic sensitive subscriber plant costs. New technology is continually adding new ways to pick up and deliver traffic—satellite services, cellular radio and digital termination systems, to name only a few. Microwave facilities can also be used. Using these means to originate and terminate long distance services, however, often means *not* using local exchange company facilities. When toll services are priced at levels which help support service to high cost areas, there is a danger that the local exchange companies will be bypassed by carriers or customers that want to avoid paying a share of the costs of nationwide service. This threat has come to be known as "uneconomic bypass."

The FCC has opened the door to competition of all kinds, but it did not find a way to solve the problem of uneconomic bypass without sharp increases in rural and residential rates. Instead, the FCC decided to make *customers* pay most of the subscriber loop costs that toll services used to help support. The FCC realized that this would be a heavy burden on subscribers in high cost areas. It said that it could protect them with a nationwide fund. But when it came to designing the fund, the Joint Board left with that duty also bowed to pressures to limit size of the fund to prevent bypass. Customers have to pay these interstate access charges in addition to their local rates. Moreover, the FCC urged the states to follow its plan in setting state access charges. This would add another additional monthly charge. If New Mexico does that, and doesn't provide some further fund, I have not been able to calculate what my customers will have to pay per month for their telephones before they make a single call. But I know it will be high because I know it takes $115 per month per subscriber to cover my fixed operating expenses. I believe that many of my customers will disconnect from the network if their rates climb too high. That does not take away the costs, so the rates for those that remain must go up. This vicious cycle threatens the very financial viability of my company. It also threatens the security of my REA loans. In other words, I am afraid that rural telephone companies like mine will be fighting for survival. This, in a nutshell, is why the nation's telephone customers are looking to Congress for help. This is also what I mean when I say the FCC has brought us competition, but seems to have lost the ability to protect universal service. For those reasons, NREATA believes that prompt legislation is an absolute necessity.

NREATA and the other Rural Telephone Coalition organizations see several points that legislation should cover. First, Congress should overturn the FCC's decision that the nation's customers have to pay so that long distance carriers may obtain virtually free local distribution service. Second, costs over 110 percent of the national average should be spread over the nationwide network, so that high quality and affordable service will remain available even in high cost areas. Third, all users and providers of interexchange service, including bypassers, should pay a fair share towards keeping our nationwide network healthy. Fourth, a support mechanism that prevents substantial disparities intoll rates should be adopted. Fifth, national policies should promote consistency in rates and services rather than jurisdictional clashes.

-1. CONGRESS SHOULD REMOVE THE BURDEN OF PAYING ACCESS CHARGES FROM TELEPHONE CUSTOMERS

The FCC's end user charge policy shifts a heavy cost burden to telephone customer, particularly if the states follow the same plan. The FCC though that the national average for interstate access charges would be about $8. The additional monthly burden on subscribers, on the average, would at least double with the addition of costs allocated to the intrastate jurisdiction. The burden on customers in high cost areas will be much greater than the average impact. The FCC's reason for shifting these costs to individual customers is that they "cause" the costs. This notion totally overlooks the nationwide character of our telephone network. The ability to reach subscribers throughout the country benefits everyone. Indeed, respected economists have shown that the widespread availability of two-way services has economic benefits for both rural areas and for the economy of the nation as a whole. Also, the idea that interexchange carriers should be able to obtain the services of local exchange companies to pick up and deliver their traffic almost free, while they make a profit on the end-to-end service makes no sense at all. Judge Greene was highly critical of this approach, and we agree. We urge Congress to eliminate the end user access charge.

2. COSTS THAT EXCEED 110 PERCENT OF THE NATIONWIDE AVERAGE COSTS FOR LOCAL EXCHANGE AND EXCHANGE ACCESS SHOULD BE SPREAD OVER THE NATIONWIDE NETWORK

We believe that the nationwide network can best be preserved in the new competitive environment by policies that keep the rates in rural areas from climbing to levels that are disproportionately high compared to the rest of the country. To this end, NREATA and the Rural Telephone Coalition have long endorsed the recovery from a universal service mechanism of a company's nontriffic sensitive costs in excess of 110 percent of the nationwide average. We also believe that such a system will prevent access charges for rural areas from becoming so high that (a) toll rates for existing service will be deaveraged to the disadvantage of rural Americans, and (b) no competing carriers will have an incentive to serve rural areas. Maintaining reasonable access charges gives rural Americans a better change of receiving some of the benefits which competition can provide and participating in the Information Age.

3. CONGRESS SHOULD SOLVE THE UNECOMONIC BYPASS PROBLEM BY REQUIRING THOSE WHO SUBSTITUTE OTHER ACCESS TO CONTRIBUTE A FAIR SHARE TOWARD AFFORDABLE NATIONWIDE SERVICE.

Universal service at affordable rates throughout the nation is a longstanding and sound national policy. The growth of competition and the introduction of new technology should be encouraged, but new communications sources should not be chosen simply as a way to avoid paying part of the costs of maintaining the nationwide network. Users of alternatives to the local exchange companies' facilites should, therefore, pay a fair share of the costs of affordable nationwide service. That way, when new technology is used, it will be chosen for its efficiency and service characteristics, not just because its price appears more attractive than the price of facilities that contribute to nationwide service.

To make the bypass contribution requirement effective, heavy penalties should be imposed for noncompliance or concealment.

4. THE UNIVERSAL SERVICE MECHANISM SHOULD ALSO PREVENT TOLL RATE DEAVERAGING

We believe that the traditional use of nationwide and statewide uniform rates has been beneficial to the nation as a whole. It promotes national unity and economic development for all areas. For more isolated farm or ranch families, telephone service can be an essential link to the rest of the country.

The era of long distance competition creates extreme pressures towards deaveraged toll rates. We strongly recommend that the national asset of network-wide prices be preserved through the Universal Service Mechansim.

5. NATIONAL TELECOMMUNICATIONS POLICY SHOULD PROMOTE CONSISTENCY AND HARMONY BETWEEN STATE AND FEDERAL REGULATION

The interests of the telephone industry and American consumers are best served when state and federal regulatory actions are not in conflict. In setting policy to safeguard universal service at affordable rates, Congress should be mindful of the obvious benefits of consistent policies and requirements.

In conclusion, NREATA appreciates this opportunity to provide its views to your committees. We stand ready to assist in enacting legislation to protect the American ratepayer and wholeheartedly support your commitment to universal service at rates that rural and residential subscribers are able to pay.

Chairman DINGELL (presiding). Gentlemen, the committee thanks you for your very helpful testimony.

The Chair will recognize my colleagues now.

My good friend Mr. Swift.

Representative SWIFT. Thank you very much, Mr. Chairman.

I suppose for some of us who have worked very hard with the independent telephone companies over a number of years to try and help achieve ends which we also thought made a lot of sense, it is a little astonishing as we march up the hill that we may be able to meet the crest of, and to find a bunch of you marching back down.

Why is that, Mr. Snedaker?

Mr. SNEDAKER. You say that there seems to be a split, is that it, or that passing legislation back awhile?

Representative SWIFT. I will be a little more specific.

The first major alarm that was brought to me was brought by one of the major independents about the access charge fee. He said it was terrible. He said it was awful and would destroy everything.

We have now come up with legislation that will prevent that from happening and that particular company, and a number of others are now alarmed that we are doing what they originally told us had to be done.

What happened?

Mr. SNEDAKER. I do not know. I would be speaking for the majority, I would say, of the independents in the industry, that this subject is not a new one, that docket 78-72 has been around for a long time, but I think the realization of the impact on some of the smaller companies just started to come to a head within the last several months, and I think the concern as expressed here—and it is a legitimate concern—is a function of a major change that could have a big impact on the high-cost companies, and also lack of knowledge which we all had as to what was in the FCC order, what did it mean.

When you read the first issue of the order, you had to read it three or four times, and a lot of people were not up to speed. USITA was holding meetings as recently as 2 or 3 months ago to educate people, and there are a lot of people that still do not understand exactly what is happening.

Representative SWIFT. I see. And so as soon as these other people really understand as well as you do, then they will all agree with you; is that correct?

Mr. SNEDAKER. I would say this, that when we first looked at it we had the same reaction they did.

Representative SWIFT. I know you did.

Mr. SNEDAKER. It was a very big concern. This is going back 2 or 3 years.

Representative SWIFT. Could I ask—I do not mean to cut you off, but I think we have a sense of your answer.

First of all, with USITA, how are the dues paid?

Mr. SNEDAKER. Each company pays dues based on their income, their revenues.

Representative SWIFT. So you are dominated by the big independents.

Mr. SNEDAKER. No, the board is—you do not base the votes on dues—the votes are one vote per person, and the board has a majority of the smaller members on it on purpose.

Representative SWIFT. So most of the money comes from the big guys, but you are perfectly happy to let the small companies dominate the board—boy, if I buy that, USITA, you would sell me a bridge, would you not?

Mr. SNEDAKER. If we did it the other way around, the small companies would pull out. They do not want to be dominated, and the larger companies do not want to dominate.

Representative SWIFT. Let me lay out a hypothesis for you, and you tell me what is wrong with it.

It seems to me that the independent telephone companies, big and small, have been living an anxious life for a lot of years now. Bell has largely been dominating this whole process. It seemed impossible for Congress even to go to battle with them and win. The uncertainty has, I think, just driven your planners crazy, and that at last came an access charge, and good, bad, or indifferent, it was settling things now. It had some certainty. You knew what the parameters were. And there just had to be an attitude in boardrooms, particularly of the larger independents, of saying just go with it, get the uncertainty over, and you know, we will do better with that than this uncertainty continuing forever and ever and ever.

Did you not feel that way? I mean is that not part of the support of this access charge?

Mr. **Snedaker**. Certainly. One of the key—I agree that the certainty is a very important part.

Representative **Swift**. I think that is legitimate. I am not criticizing that at all. But I am trying to understand the thought process that would get what to me is a fairly dramatic about-face on the part of at least the larger independents.

Mr. **Snedaker**. Well, I would say again that if we went back and looked at our filings in docket 78-72 over the last 3 or 4 years and you could see a gradual shifting in our position, and you started to think about the bypass issue and how you really should attack this.

Representative **Swift**. Now, I think that is good.

Mr. Chairman, if I could prevail on you just a little bit.

Chairman **Dingell**. The gentleman is doing just fine.

Representative **Swift**. I always find it important to ask the right questions if you are going to get at the right answers. I remember staying overnight at a hotel, I had a speech to give that noon and wanted to check out, put my bags somewhere, and I was just going to grab them and run right after the speech. And I went down to the lobby, paid my bill and had my bags, and I saw this little fellow in a very snappy uniform there, stood about so high, and I went up to him and said, what can I do with these bags so I can get them later, and he said in this startling Australian accent, well, mate, the first thing I would do is ask a bellhop instead of an airline pilot.

Now, it seems to me the kinds of questions that could be asked about dealing with bypass, that is key, bypass is key, and the kinds of questions that were being asked grew out of who was asking the FCC that has a rather rigid philosophy in this regard, and telephone companies. And if you said, boy, if you charge access fees to the long-distance companies, you have got this bypass problem, how can we resolve that, and I think the kinds of questions that those particular people, honorable all, but with their particular perspective, they would be asking questions that would probably lead you to sticking it all to the end-user. This is the one person that was not involved in all of that, that was the end user.

I just think there were some questions about how to handle bypass that never got asked. And, therefore, you did not get answers that might resolve that bypass problem which has to be resolved in a fashion that does not lay it all on the end user.

It seems to me that that flows pretty logically.

What we are trying to do in Congress, because we are supposed to represent those consumers, we have asked some other questions. We are saying if you have got a bypass problem and you have to resolve it, how do you do it without sticking it all on the end user?

We have come up with this proposal with regard to charging a fee to the bypassers that will neutralize access charges as part of their economic analysis to decide whether or not they are going to bypass.

While I can understand you people's almost desperate need for some certainty in this process so you can get on and deal with all of the other revolutionary things that are happening, I understand that, but it seems to me it is not asking too much to just let us go 6 months more with a little uncertainty so we can take care of that end user, the consumer, as well.

I really feel that after some of us hung in as long as we did with the concerns of the independent telephone industry on this whole long process, to find you bailing out because you have got your part of the problem at least under control, if not solved to your total satisfaction, is unfortunate at best.

I just appreciate, if you want to respond, I am interested if any of the other panelists have any comments on this analysis that I just went through.

Mr. SNEDAKER. Certainly it is of help. It is one of the concerns in the bypass, as we heard today, is the message, the clear message to the people that want to become bypassers or think they should because there is an economic incentive there, and if the message is there, why go out and build your own facilities when we have facilities here that you can use, and the only reason you leave is because you want to avoid the toll subsidy, that then puts a further burden on the existing customer.

So that is one point that came to us as we started internally to debate it just among two or three people in our company. And we are not probably as susceptible to bypass as New York Bell or Illinois. Our largest town is 50,000.

But nonetheless, if you take Tennessee Eastman out of Bristol, Tenn., or one of the other two large customers, that will have a major impact on those areas. So we were interested and concerned about that.

We do have some problems, the same problems that were discussed today with respect to measuring bypassers and what was their intent and so on and so forth with respect to the charges or what have you, the fines, or which way you go, and we think that could be very difficult.

Representative SWIFT. Obviously there are some problems there, but they can be solved. And I think the problems you might have there are at least equal or are no more than equal, maybe less difficult than setting up the whole welfare system that seems to be the logical followup if we implement the access charges.

I would be interested if any of the other panel members would like to comment on the observations that I made.

Am I all wet?

Mr. WARE. Congressman, the small company segment of the industry I think wholeheartedly appreciates the efforts that many in Congress have made to try to protect the interests of the consumers, and I guess because of our size we feel that we are closer to the consumer and also very concerned. So we support this effort at legislation which would prevent the escalation of local service rates beyond the means of many of our customers.

I guess we have been fairly consistent in that position all along.

Representative SWIFT. It seems to me you fellows need some stability in this industry as badly as the big guys, but you are willing to hang in there one more round to see if you cannot get a better deal for the consumer.

Is that fair?

Mr. NEHRING. Congressman, I might add, being a part of the USITA picture for a number of years, I think there has been a serious effort made to accommodate and reach consensus. But as you touched on, when the mantle of AT&T and the overall partnership started to break up, I think everyone was immediately forced to look at their own self-interest, just as I must.

As a result, those companies with a small base, with the inability to flex, to transfer their investment, like basically we are, will have a different attitude than someone like a General Telephone or perhaps a United. We have really nowhere else to go. We are looking at a laboratory model, like I explained earlier. That is it. There is no option for most of us.

So there is a difference there, and I think it just demonstrates another reason why Congress must come up with a national policy to hammer perhaps some consensus that will not be achieved in the industry. I think they have the talent, if they ever get pulling in one way, to work with the regulators to resolve the matter. I think the regulators also need some direction because there are some varying degrees of participation in the regulatory field from the State standpoint.

I think that is why the sooner Congress does take that step, the better off the whole Nation will be.

Representative SWIFT. Thank you, panel.

Mr. Keen, did you care to say something?

Mr. KEEN. Yes; I would like to say a word or two about that same thing.

I, too, belong to USITA, and I have worked in their small business committees and things like that. I have no falling out with any of them, but we do not always agree with everything. We are kind of like a big family, you know. We do not always think alike.

Some of the thinking of some of the larger companies would bankrupt my company, so I cannot go along with them, naturally. Yet I do not fall out with them. They are running their show and I am trying to run mine.

Talking about positions, now, we were just looking at a piece of paper back there a while ago that the Rural Coalition put out in 1979, and I read it a while ago, and I still has not changed anything, any of my thinking on it. It looks just like, you know, we still have the same problem. It has not changed any.

You know, when you are operating a company like Rollie or my own or anywhere where it is in a real rural district—and when I talk about rural, some people in this room may not know what I am talking about, and my idea of universal service may be a lot different from some of the other people in the room. Mine do not stop on pavement. It goes on out to the far end of every creek in our area. It has run the cost up tremendously, but they have all got a phone out there that wanted one within my certificated area. It was very costly to do it, but that is what it says in the REA contract that I signed with the U.S. Government—that we would do that. And most REA bars have done that.

Now, that is universal service, when anybody out there, rancher, farmer, miner, or whatever that needs and wants a phone can get one. He has also got to afford it. Now, if it starts running too much, a lot of them cannot pay for it, and the rest of them will not pay for it.

And there again, you are getting away from universal service because it should be where anybody, basically anybody, could afford at least a telephone that they can call in on. I do not think that measured service, you know, is necessarily the way to go, but it could be done that way.

We could also, you know, if someone did not want to pay their toll access charge under the FCC plan, well, there are ways that we could separate that and not make the customer pay. We can deny them toll, but it is a real problem to try to figure out how to recover under the FCC plan that just simply turns everything over to the customer. I do not think that is a solution.

Chairman DINGELL. When you say turns everything over to the customer, you mean, turns all the charges over to the customer.

Mr. KEEN. That is what I am talking about.

Chairman DINGELL. That is different from benefitting them.

Mr. KEEN. That is what I am talking about, is the access charges. You are saying, for instance, in New Mexico, the intrastate charges are not going to be pooled. That is, under the present plan that Bell has presented, and that would mean that our company, that the nontraffic-sensitive costs are certainly out of the question. Anybody paying those per month, any customer, just simply means that we have got to be pooled. Otherwise we are dead in the water

Chairman DINGELL. Would the gentleman yield here?

Representative SWIFT. Certainly.

Chairman DINGELL. Mr. Keen, if the FCC ruling had been in place when your particular telephone company was started, how many of your subscribers would have telephone service now?

Mr. KEEN. I do not believe I would have bought that company.

Chairman DINGELL. I do not believe that there would have been any company for you to buy.

Mr. KEEN. That is probably right.

Chairman DINGELL. If you had to start your company now under the FCC ruling, how many of your current subscribers would you be able to serve, and how many of them would be able to afford the kind of service that you would have to provide at the kind of rates that the FCC plan would require?

Mr. KEEN. That would be hard to say, you know.

Chairman DINGELL. Would it be fair to say that all of the subscribers would be delighted with the rate?

Mr. KEEN. No way.

Chairman DINGELL. What are you telling me about that?

Mr. KEEN. I think on probably about the second or third year, that we would drop out quite a few customers. We would drop out some immediately, let's say, but then as it got close to a total of $25, or $30, $40 a month, they are not going to pay that.

Chairman DINGELL. What would your rates be under the FCC regulations as set forth?

Mr. KEEN. Let me quote what REA said in 1981. They used 1981 figures on all of the companies in the United States, and mine happened to be No. 9 on the hit parade or something like that as high cost, $108 a month would be the total revenue requirement. The customer would pay $43.99, I believe it was, or $44 a month. That is at the end of the 5-year period, or 6, whatever, the end of the transition.

Chairman Dingell. You are saying it is $108 or $44?

Mr. Keen. I said the total revenue requirement was $108, and the customer would be paying $43.99 of that.

Chairman Dingell. Who would make up the deficit?

Mr. Keen. We have a good many traffic-sensitive costs, you see, that come out of the settlement.

Chairman Dingell. I see.

Mr. Keen. That is where it would come from.

Chairman Dingell. Mr. Copsey, how many of your subscribers would be receiving service today? How many of your subscribers would be able to start up if you were starting up your company, as subscribers of your under the FCC's proposed regulations on this matter?

Mr. Copsey. If I were to do the thing over today and build that, I think the customers that would end up and have service would be those in the town portions and basically the very close perimeter to town. The rest of them in the rural areas would not have service.

Chairman Dingell. What would your rural and city subscribers be paying per month if you were to be stringing lines and hooking up your customers today under the FCC regulations?

Mr. Copsey. I have never really tried to do that, figuring what to go back to, but I do know that to hook up a new—each additional customer that we hook up today is in the range of $1,500, that cost. But you have got a lot of imbedded costs in there that are greatly depreciated. So then effectively it brings it into line or makes it a lower amount that then is meltable to the other.

Again, I have not added up and tried to put that into a meaningful bid, or trying to assume I wanted to start over from scratch in a rural area. I just do not think that the rural people would ever end up and receive service under today's costs.

Chairman Dingell. You mean with the regulations that the FCC proposes?

Mr. Copsey. Yes, with 78–72 implemented.

Chairman Dingell. Mr. Ware, what comment do you have?

Mr. Ware. I believe the subscriber base would be limited to the confines of the small communities. Our company is a cooperative, and we serve 24 very small communities. The exchanges range in size from about 110 subscribers on up to about 1,400. And our system is financed almost entirely with REA loan funds, and REA is required to determine that the loan is feasible before they will lend funds.

Chairman Dingell. In other words, the loan could be repaid.

Mr. Ware. Yes, so that the loan could be repaid. So I would doubt that many of the improvements that have been made would have been made under present or proposed regulations.

Chairman Dingell. What are your current monthly charges, Mr. Keen, Mr. Copsey, and Mr. Ware? What will they go to if the FCC's plan goes into place?

Mr. Ware. It is very difficult to determine exactly, but our weighted average rate, taking into consideration the different rate levels we have, is $6.40 a month.

Chairman Dingell. What will it go to if the FCC's plan goes through?

Mr. **Ware**. Could I comment just on the $6.40 for a moment, Mr. Chairman?

The $6.40 appears to be very low, and that is because our exchanges are very small, and many of our subscribers can only call 500 other subscribers without paying a toll charge.

Now, the projected rate under the proposed FCC rules would be about $22.50, approximately 250 percent increase, and we are fairly certain that many of our subscribers cannot pay that, which then generates the rate spiral and further disconnection that the committees have heard about.

Chairman **Dingell**. Mr. Copsey, what do your subscribers pay now and what would they pay if the FCC plan goes into place?

Mr. **Copsey**. Because the FCC plan has evolved on through here and is necessary for each of the small companies in many states to file their own access charges, we have derived what our costs are. The national average nontraffic-sensitive costs per year per loop, revenue-producing line, is $227, and those are varied all over the place, we have heard, but this was put together by the industry recently and I think is the new figure that will be used for 1984 costs.

By the same token, we end up and got our costs together, and our same nontraffic-sensitive costs were $228 per year, which says that we were right on the average.

Chairman **Dingell**. This is the average cost per subscriber?

Mr. **Copsey**. Yes, and the national average was $227. So taking that and dividing it by 12 months gives you $19 a month that you would end up to the customer. The remaining costs that would be there, they are in the form of traffic-sensitive costs, and I do not know what those would amount to.

Chairman **Dingell**. What would your subscribers' rates go to under the FCC's plan?

Mr. **Copsey**. I am going to guess. They are currently $9.35 for residential. They would end up and add, prior to yesterday, it would end up and add roughly $4 per customer for interstate access, and if you mirrored that on the State side, you would have about $3. So this is the start of the transition, not to the end result. So that would be $7 onto that, would be $16.35, in that neighborhood.

Chairman **Dingell**. And it will escalate as the years go by.

Mr. **Copsey**. Yes.

Chairman **Dingell**. At about what rate per year?

Mr. **Copsey**. Because we fell right close to the average, it looked like that probably 3 years would end up to get us into the $19.35 and then some. I assume $19.35.

Chairman **Dingell**. $19.35?

Mr. **Copsey**. Yes, for the nontraffic-sensitive portion. You send up and have a traffic-sensitive portion.

Chairman **Dingell**. And that would raise it by how much more?

Mr. **Copsey**. I really do not have a feel for that. I would guess in the range of $5 or $6.

Chairman **Dingell**. So that would carry it to $25 a month.

Mr. **Copsey**. $24 or $25 I think would be adequate.

Chairman **Dingell**. Mr. Keen, what are your present monthly charges, and what would they go to under the FCC regulations?

Mr. **KEEN**. It is about $7.75 right now. We have a rate increase filed for $10 across the board for the whole system. Of course, we have a brand new system, and so we are asking for the new rates on account of the new service that we are giving them. It is not a very fair—it is very low because the previous owner had not asked for a rate increase since 1959. So we had to wait until we rebuilt the system, and then we went in for a rate of $10.

Chairman **DINGELL**. You mean a total of $10?

Mr. **KEEN**. Yes.

Chairman **DINGELL**. Now, if the FCC's plan goes into place, that $10 rate would rise to what?

Mr. **KEEN**. Well, $2 for the first year for interstate access, that's $12, and then I think that is about $3 for intrastate.

Chairman **DINGELL**. How about traffic-sensitive charges? What would these charges raise it to?

Mr. **KEEN**. The first year the customer would probably not be raised up over about $16, $17.

Chairman **DINGELL**. And the second year?

Mr. **KEEN**. Well, just whatever, it raises $2 a year, was it not? It would probably do the same thing on the other side. So it probably would be raised about $4 a year for 4 or 5 years, to the end of the transition period.

Chairman **DINGELL**. So you are looking at something on the order of $17 the first year, $21 and $25 or thereabouts, in the second and third years respectively, is that correct?

Mr. **KEEN**. I believe that is right.

Chairman **DINGELL**. Mr. Nehring and Mr. Snedaker, could you please tell me what are your current average charges per customer, and what would they go to under the FCC's plan?

Mr. **NEHRING**. Mr. Chairman, right now, we have average local rates. Our average local rates are around $11.

Chairman **DINGELL**. And what would it go to?

Mr. **NEHRING**. I would like to add to my opening testimony. Most of the studies have been done this way, by assuming transition was completed. We take the position that a wolf is a wolf, even though there is a sheep's wool draped over it. Although the transition is desirable, that the end result of the end user, customer, still paying everything for the nontraffic-sensitive costs is really the study level. The REA study has been done that way also. Most of the studies I have done have been done using the most current figures available, but assuming the transition is completed.

On that basis, depending upon how some of the interpretations of the debt equity ratio paragraphs of the joint board and so on are interpreted, our monthly rates will range from a high of $49, and the example I gave, using a totally different approach, came out $47. But once again, that assumes total transition also, compared to REA's figure of $37 per month which would include all access charges and local charges upon completion of transition.

Chairman **DINGELL**. Mr. Snedaker.

Mr. **SNEDAKER**. In the United Telephone system the average is about $10 a month right now, and obviously the first year you would go with $2, but that $2 would go up to $4, and you would have it matched on the intrastate side probably at about $4, so you go to about $18, and then it would be offset, the total bill would be offset by any reduction in toll, which averages about $30 per customer.

Chairman DINGELL. About what?

Mr. SNEDAKER. About $30, if I figure it correctly.

Chairman DINGELL. So your $10 monthly charge would go to $30?

Mr. SNEDAKER. No, the local rental, $10, would go to maybe about $18, but then I am saying at the same time today you pay $10 on a local, you are running $30 in long distance, let's assume, and that $30, if there is any reduction that has been predicted here today, that will be an offset downward.

So today the total bill would be $10 plus $30, which is $40, and then you go up to say $18, and then you take the $30 and say if there is a reduction for the same volume, it would reduce the bill by that amount. There would be an offset.

And then the other offset which we have not discussed is the high cost fund, and I do not know if that has been priced out.

Chairman DINGELL. Your assumption is that your people are going to be using long distance fairly extensively, correct?

Mr. SNEDAKER. I would say on average; you have the high users, you have the lower users, and you have the people that do not use it at all.

Chairman DINGELL. What about the little guy who does not use much long distance. He is paying $10 now. What is he going to pay at the end of the transition period?

Mr. SNEDAKER. If he makes no long distance calls, he will pay $10 now. He will go up to about $18.

Chairman DINGELL. I beg your pardon?

Mr. SNEDAKER. $18 at the end of the transition.

Chairman DINGELL. All of this is going to occur because the nontraffic sensitive costs of the local plant will be loaded entirely on the local subscribers, is that right?

And right now that does not happen, does it?

Mr. WARE. No, that is correct, Mr. Chairman.

Chairman DINGELL. That enables your customers, Mr. Copsey, Mr. Keen, and Mr. Ware, to have widely available telephone service at reasonable cost, is that correct?

Mr. WARE. That's correct.

Chairman DINGELL. So the FCC's plan would change that, is that correct?

Mr. WARE. Change it drastically, and probably to the detriment of our customers.

Chairman DINGELL. The congressional goal set forth in law as universal telephone service is part of the 1934 act, is that correct?

Mr. WARE. That is correct, sir.

Chairman DINGELL. And the FCC would change that?

Mr. WARE. Yes, sir.

Chairman DINGELL. Now, why should we do that?

Mr. WARE. As our testimony indicated, Mr. Chairman, we do not believe that should occur.

Chairman DINGELL. I join you enthusiastically in that statement.

Maybe Mr. Nehring and Mr. Snedaker can tell us why we ought to make that change.

Mr. NEHRING. For the record, Mr. Chairman, I agree with these gentlemen.

Chairman **Dingell**. Now we are making progress.

Now, Mr. Snedaker, why don't you tell us why we should make that change?

Mr. **Nehring**. I totally disagree with a total change of philosophy. For years we have heard the hue and cry of toll subsidizing local, and all of a sudden we come up with an 180 degree turnaround pendulum swing whereby the local is going to be paid totally by the end user, after the transition, and all of a sudden "little" companies like AT&T and IBM and ITT and MCI are going to be able to come to our customers free, so to speak, because the customer is already paying for that local cable.

Chairman **Dingell**. And you are providing the local amount that is going to make that interstate system for these big folks desirable, cheap and accessible.

Mr. **Nehring**. It makes it easier for them to make a profit. I really—bypass certainly is something that is a problem for a lot of the companies.

Chairman **Dingell**. Bypass can be addressed, can it not?

Mr. **Nehring**. I think it can, and very frankly, I do not know if the FCC bill will cure it because it is so transitional itself that bypass, by everyone's statements here today, is moving so rapidly that if we are going to transition to the FCC plan, bypass will have occurred before the FCC plan can get those end user costs to the end user.

Chairman **Dingell**. That is right.

Now, there is also another thing. The FCC plan will encourage bypass of the local system, is that not a fact?

Mr. **Ware**. That is correct.

Chairman **Dingell**. Gentlemen, our reporter cannot get nods. You have to say yes or no.

Mr. **Ware**. Yes, Mr. Chairman, and could I address another point that has been addressed several times today, and that is that the alternative for individuals who cannot afford the newly priced local service could have measured service, and that is not a viable answer for many of us who have small exchanges. The investment required to even measure the service would be substantial, and our exchanges are so small that you do not have a sufficient subscriber base over which to average the costs that are not being recovered.

Chairman **Dingell**. All right.

I am sorry, Mr. Copsey. Go ahead.

Mr. **Copsey**. May I add one more confusing bit to that?

Chairman **Dingell**. We do not want any confusion here. There is enough in the record already.

Mr. **Copsey**. The FCC plan where the end user pays for all of the nontraffic sensitive costs after the transition period, taking that in my eyes is absolutely absurd. I have heard three or four times today that LMS or local measured service is a method to provide lifeline service or to see that everyone has universal service. Bear in mind that the rationale, the economic rationale that was used to get the end user to pay for the nontraffic sensitive costs in the FCC plan, those are the same costs that make up the local measured service costs. Yet, on local measured service, you end up and you apply all usage to those same costs.

So you have got two opposite directions there of people talking from both side of their mouths.

Representative **Gore**. Would the chairman yield for a brief comment?

Chairman **Dingell**. Sure I will, of course.

Representative **Gore**. It seems to me measured service, as it has been described in these circumstances, is a substitute so long as you do not use your telephone.

Mr. **Keen**. That is right.

Mr. **Snedaker**. I think measured service gives the customer a choice, gives him a choice in a way.

Representative **Gore**. Of using it or not using it.

Chairman **Dingell**. Or of dropping it if it costs too much.

Mr. **Snedaker**. It gives him a choice, which is important, I think.

Representative **Gore**. It seems to me, Mr. Chairman, if I can make another short comment, that this problem is similar in accounting terms to one which faced railroads years ago, when they took the joint and common costs of maintaining tracks and equipment in order to meet competition from other carriers, shifting all of the joint and common costs they could from freight onto passengers, and that in some measure accounts for the state of passenger service in the country today.

My concern— and I know you all have expressed this as well— is that you are going to see a lot of local telephone customers going the same route and just not being able to be a part of the system. We see them in our congressional districts, and we talk with people who have social security disability or some problem, you know, they are 4 or 5 percent of the people, just cannot afford a telephone today, but not that many. But that number, particularly in rural areas, is likely to jump way on up there.

I appreciate the chairman yielding.

Chairman **Dingell**. I apologize. I will recognize the gentleman as quick as I can.

Gentlemen, each of you on your exchanges have a few very large companies that use part of your facilities within your local service net. Who might be encouraged to bypass your met if the local access charges get too high?

Mr. **Ware**. We are very limited in the number of large customers in our small communities, but when the local service rates go that high, there is the danger or the probability of local bypass, as you have mentioned, and that would be very real, and that would work to the destruction of the local exchange concept.

Chairman **Dingell**. It would also cause an enormous drop in the revenues because it would pull a lot of calls that are now going through that local exchange out of that exchange.

Mr. **Ware**. That is correct, Mr. Chairman.

Chairman **Dingell**. It would cause further cost escalation for the remaining subscribers who do not have the resources to bypass, would it not?

Mr. **Ware**. Our particular company does not have as large a potential for that as many of the other small companies in the United States, but for many, it is a very real problem, as you have mentioned.

Chairman **Dingell**. How about you, Mr. Copsey or Mr. Keen?

Mr. COPSEY. We have been very fortunate and have experienced a great deal of bypass over the past few years, and I say that because from our eyes, what the Bell system has done to us is the same thing as what the Bell system is saying that MCI and others would be doing to them in the form of bypass. The message toll has ended up and been converted to private lines, FX's, this other type of stuff. So we have already experienced a great deal of bypass.

Chairman DINGELL. Mr. Keen.

Mr. KEEN. We have two customers in our operating area that would probably be subject to bypass.

Chairman DINGELL. Who would they be?

You do not have to identify them by name, but just give a description.

Mr. KEEN. Well, one is a big radio-telescope project that is scattered out over 30 miles out there on the prairie.

Chairman DINGELL. They could attempt bypass?

Mr. KEEN. They could probably come out with bypass. And then we have got the Air Force and FAA at a radar site that might bypass.

Chairman DINGELL. And they would be tempted to if your local access charges got too high.

Mr. KEEN. Right.

Chairman DINGELL. Mr. Nehring, what kind of experience do you have?

Mr. NEHRING. We have in most of our areas at least one or two major users, a large ranch, the Forest Service. This was a few years ago, but the Forest Service wanted us to look into giving them FX service which, as you know, puts that phone into the nearest Bell town and leaves us with the extension, and it would have impacted us 33 percent just from that one customer.

Chairman DINGELL. As I gather it, the FCC's plan could very well exacerbate that situation, could it not?

Mr. NEHRING. I think our biggest—we as small, rural independents pay the price for competition, but we basically do not get much of the benefits, and our biggest bypass threat is probably from the adjacent Bell people. It is in their self-interest to try to get that revenue.

Chairman DINGELL. Mr. Snedaker, do you have any comments?

Mr. SNEDAKER. Yes, I do, Mr. Chairman. As I understand the thrust of the question, we are talking about the FCC placing access——

Chairman DINGELL. Encouraging local bypass, not bypass of the——

Mr. SNEDAKER. No, local bypass, correct.

Now, I guess I would suggest the cases we just talked about may be considered local bypass, but the local bypass, in my opinion, would only take place if you have an alternate facility there, and that the cases we are talking about really are customers that are attempting to bypass the toll.

Chairman DINGELL. Let's suppose you had a cable system that was able to provide communication services, or let's suppose that they could hook into some kind of a microwave system.

Mr. **Snedaker**. Then that would obviously today be an exception rather than a rule, particularly in the rural areas that we are talking about.

Chairman **Dingell**. If you get enough folks with high local access charges, you are going to find that bypass is going to grow, are you not?

Mr. **Snedaker**. I would say possibly, although it is very costly to convert CATV systems to have the capability of two-way switched voice.

Chairman **Dingell**. They are planning it right now.

Mr. **Snedaker**. Right, but in the big cities, primarily, the major markets. But if you did have that capability, obviously, and it drove the access charge up high enough, you could drive the customer onto an alternate network, if it were available and if it were cheaper.

Chairman **Dingell**. Thank you.

Gentlemen, the Chair thanks you. I have kept my friend and colleague, Mr. Gore, waiting too long.

Representative **Gore**. Thank you very much, Mr. Chairman. It is fine. I have enjoyed the interchanges.

I would like to ask you a couple of questions, Mr. Copsey.

What percentage of your revenue do you get now from long distance contributions?

Mr. **Copsey**. Approximately 60 percent.

Representative **Gore**. Sixty percent?

Mr. **Copsey**. Yes.

Representative **Gore**. The other 40 percent comes from your local ratepayers.

Mr. **Copsey**. Yes.

Representative **Gore**. Under the FCC plan, you would have to charge your customers $2 going up to $6 for long-distance access, right?

Mr. **Copsey**. Yes.

Representative **Gore**. Now, would that make up for the reduction in the amount of contribution that you get from long distance?

Mr. **Copsey**. No, it will not.

Representative **Gore**. Well, over what period of time—well, in other words, some people have the notion that this lid that the FCC has put on is going to put a lid on the impact on customers that comes from the restructuring of access charges, but that is just not so, is it?

Mr. **Copsey**. That very likely is not so. I have not seen the order, and I doubt that the order has been written yet. But when it does, that is a very critical point, because they may very well end up and lower the interstate revenue lid, cut it from $4 down to $2, but then you are going to find yourself with a $2 shortfall on the State side that will then necessitate all companies going in to recover that revenue shortfall from the State jurisdiction.

Representative **Gore**. So you will be under pressure to raise local rates over and above what these other pressures are causing in order to make up for the lost revenue that you are now getting from contributions.

Mr. **Copsey**. That is very likely to happen. But then that would come from the deciphering of what the order, the new order says.

Representative **Gore**. As I understand it, that 60 percent which you now get would go down to 25 percent.

Mr. **Copsey**. At the end of the transition.

Representative **Gore**. And then the $2 went up to $6 initially, but there is going to be a mismatch in your case. Supposedly at the end of this interim period the charge on the customer is supposed to equal the 25 percent in what you have lost, but it will not in your case.

Now, we have heard a lot of talk today about the potential problem of customers in urban areas subsidizing rural and high cost areas. One of our colleagues referred to these as gold-plated services.

I just wanted to ask you, Mr. Copsey, could you give us your estimate of how many small telephone companies in OPASCO, for example, are flush with cash and offering gold-plated services to wealthy farmers, for example?

Mr. **Copsey**. First I would like to know where the wealthy farmers are at this stage of the game.

But you keep running on to this bit that the rural companies end up in gold-plate systems, build them that way. I do not think that that is really true. I think that is an adage that may have gotten on there by the actions of a few, but I do not know who those few are. But then again, as in any business, there are some that end up and lean toward that—get that name started.

However, I think—and the country I am most familiar with is Missouri—I do not know of anyone in there that would consider it gold-plated. In fact, I consider there are several in there that are quite frugal operators. And I think you will end up and find that the vast majority fall in that very category.

Representative **Gore**. We have a lot of statements around here sometimes based on mythology instead of fact, and I think there is a heavy mythological content to that gold-plated services charge.

Now, let me ask you about universal service. Do you know of any way to gage how many of your customers will disconnect from the system as rates go up, a certain percentage? We have had estimates that, for example, for a 10-percent increase in rates, 1 percent of the customers will drop off the system.

Do you know of any good evidence or any good way to estimate what the impact on universal service is likely to be in your area?

Mr. **Copsey**. There have been various studies made on that, and I think I give those about the same credence as you do, which is nearly none. I think the real experience that one has got to draw on the various local rate increases that the companies have experienced throughout the time, and they end up trying to draw from that what the disconnect rate has been.

But if you end up there and get on into the $20 range, you are into a new world out there, and you have got rural areas out here that $20 in an urban area, $20 in a rural area that is low income is a good many more dollars.

So I think whenever you talk about what percentage will disconnect, I do not know what those dollars are, but this is my own opinion, I think that they exceed 2 percent in disconnecting from the network and universal service, and brings on great problems for Congress to straighten up at that time from the public.

Representative **Gore**. We are anticipating those right now.

Mr. **Copsey**. I appreciate this.

Representative **Gore**. Anyone else want to comment on this?

Mr. **Nehring**. I would like to say it will somewhat depend on the type of exchange area that you have.

Representative **Gore**. Will you pull that microphone around?

Mr. **Nehring**. One of our exchanges is very heavy on retirees. They run on a much tighter budget than a farm family.

Representative **Gore**. And they figure it down to the penny in many cases.

Mr. **Nehring**. Many of them never make any calls. The children pay for their phone just so the children can call them and for emergencies. But the children will still support them, and that is one thing. But those people paying it themselves watch every penny, and they will be the first to drop off.

The people that do have places up in summer home areas, for example, will quickly drop off because that phone is a convenience. Maybe for them it is not that big a problem, but as they fail to support—there are people in those areas who live permanently and have health conditions, because a lot of them are retirees. So as the temporary people drop off because of migration, once again that base becomes a Catch-22.

Representative **Gore**. Well, it has cascading effect, because the customers remaining in the rate base have compressed upon them a larger share of the load, and it cascades.

Mr. **Nehring**. I feel the threshold is about a $20 rate from the few people I've talked to. You know, we have not been too anxious, up until now, to forage out there and get the people all unnerved, because the FCC formulas really had not been firmed up. They are becoming more firmed up. And it is our intention to start having open houses so at least the people cannot say "why did you not tell me so?"

Representative **Gore**. Yes.

Mr. **Nehring**. The few that I have talked to personally feel that that $20 is kind of the straw that will break the camel's back.

Now, there are some that will pay $40, obviously, but the average user out there to me looks like $20, $21, and you start losing them.

Representative **Gore**. Well, in Tennessee, just to take that as an example, our average bill is around $12.65 now, and they are proposing to go to between $28 and $29, so that will pretty well crash through that barrier which you indicate has such meaning.

Mr. **Nehring**. Yes, sir.

Mr. **Snedaker**. I would just like to make one comment based on some of the experience we had at United Telephone Co. in Ohio, which was back in 1975. At that time we had a 42 percent rate increase going from about $7 a month then to up around say $10.50.

Now, the problem you have is to determine why customers are leaving. Unless you interview them and really know—but this was during an economic downturn—but based on looking at those figures and those results, I would have to say our dropoff was probably around 1 percent, and half of those came back in 6 months. So I think it is a difficult thing to project.

Representative **Gore**. But by the terms of the example, you are still below that threshold area where people have to put it into a different budget category. Seven to ten dollars is very different than $12 to $28, a very different effect

Mr. **Snedaker**. I agree.

Mr. **Ware**. Mr. Congressman, I think our area is probably not unlike a lot of other small telephone company rural service areas, and we have a larger percentage of elderly in our area than the State average does, and about a third of the people over 65 live alone, and I think it is about 25, 26 percent of those are considered to be below the poverty level.

So I think talking about a threshold of $20 is probably adequate in some areas, but I think there are many of our rural service areas where $20 is not an affordable rate for many of the subscribers.

Representative **Gore**. Well, thank you all very much.

Mr. Chairman, I have no further questions for this panel.

Chairman **Dingell**. The Chair thanks the gentleman.

Gentlemen, you have been kept here a long time, and you have been very patient by waiting.

The committee thanks you. Both committees thank you for your assistance to us.

The Chair announces with great pleasure that I may gavel down, and I announce the next meeting will take place in the Caucus Room of the House of Representatives Cannon Building at 9:30 in the morning.

[Whereupon, at 5:28 p.m., the hearing was adjourned to reconvene at 9:30 a.m. July 29, 1983.]

UNIVERSAL TELEPHONE SERVICE PRESERVATION ACT OF 1983

FRIDAY, JULY 29, 1983

U.S. CONGRESS, SENATE COMMITTEE ON COMMERCE,
SCIENCE, AND TRANSPORTATION, AND HOUSE COMMITTEE
ON ENERGY AND COMMERCE,
Washington, D.C.

The committees met, pursuant to notice, at 9:35 a.m., in room 345, Cannon House Office Building, Hon. John D. Dingell (chairman of the House Committee on Energy and Commerce) presiding.

OPENING STATEMENT BY CHAIRMAN DINGELL

Chairman DINGELL.[1] The meeting will come to order.

The Chair welcomes his good friend and colleague, Senator Bob Packwood and our colleagues from the Senate. On the House side this morning we express our appreciation for the courtesy extended us yesterday and for the remarkable leadership that our colleagues in the Senate have extended in this important matter.

The Chair recognizes Mr. Packwood for such opening statement as he wishes to make and then Mr. Wirth.

OPENING STATEMENT BY CHAIRMAN PACKWOOD

Chairman PACKWOOD. Thank you. You know, as far as we were concerned we found the hearings yesterday very helpful. As I look at the panels this morning, I dc not think we will be here until 5 o'clock on the hearings, but all of you I hope can say that these have been full and fair hearings and that if there are any positions left uncovered, I do not know what they might be.

OPENING STATEMENT BY REPRESENTATIVE WIRTH

Representative WIRTH. Today we continue our hearings on legislation to assure the continued universal availability of affordable telephone service.

At the heart of all of the bills before us is the revision or complete repeal of the FCC's access charge order. That order, as we all know by now, would eliminate the contribution that long distance service currently makes to local service—and, as a result, raise monthly local phone bills by $8 by the end of the decade.

What is so striking about the FCC's order is its unfairness, its lack of balance. Over the years, the members of these committees have debated the prpoer allocation of the costs of local telephone facilities used for both local and long distance service. Some of us would have assigned more costs to local service than is currently the case; others would maintain the present allocation.

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[1] Representative Dingell presided over the hearing this day.

But nobody has ever suggested that long distance service pay nothing toward the costs of local service. Nobody, that is, until the FCC announced its access charge decision last December.

The legislation I have introduced, along with Chairman Dingell and other members of the committee, would restore the balance that the FCC has upset. Our bill would require the Commission to establish a new access charge formula under which long distance telephone companies and private telephone systems continue to bear an equitable share of the costs of local telephone service.

It bears repeating, however, that the legislation before us today addresses only one piece of the telephone rate issue. The multibillion-dollar rate requests pending in almost 30 States are beyond the control of any Federal legislation.

It is up to the public utility commissions in those State to carefully scrutinize those requests, and grant only as much as can be justified. I suspect that that will be far less than the $5 billion to $7 billion that is being sought.

And it is up to the Bell operating companies to make sure that the divestiture process leaves them with the proper allocation of debt and assets to start 1984 in a financially viable condition, and not in need of massive transfusions of cash from local telephone customers.

Our responsibility in Congress is to make sure that FCC decisions do not unnecessarily contribute to the upward pressure on telephone rates. That is the purpose of my legislation, and the other bills that have been introduced here and in the Senate, and that is also the subject of this morning's session.

I welcome our witnesses and look forward to their testimony.

Chairman DINGELL. The Chair announces that our first panel is a panel composed of Mr. Theodore Brophy, chairman and chief executive officer of General Telephone; Mr. Robert Flanagan, chairman of the board and chief executive officer, Western Union; Mr. Neal J. Robinson, executive vice president, U.S. Telephone Communications, Inc.; Mr. Charles L. Brown, chairman of the board, American Telephone & Telegraph; and Mr. William C. McGowan, chairman of the board, MCI Telecommunications Corp.

We appreciate your courtesy to the committee. We look forward to your testimony with interest. Gentlemen, we have very important witnesses on this panel, and our concern is that we hear your testimony in a proper and appropriate order. Do you have any order in which you would like to be heard? Then the order will be as follows: Mr. Charles Brown, Mr. Theodore Brophy, Mr. William McGowan, Mr. Robert Flanagan, and Mr. Neal Robinson.

Gentlemen, for the assistance of our reporter and for the purposes of the record, would each of you please identify yourselves starting on your left.

STATEMENTS OF CHARLES L. BROWN, CHAIRMAN OF THE BOARD, AMERICAN TELEPHONE & TELEGRAPH CO.; THEODORE BROPHY, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, GENERAL TELEPHONE & ELECTRONICS CORP.; WILLIAM C. McGOWAN, CHAIRMAN OF THE BOARD, MCI TELECOMMUNICATIONS CORP.; ROBERT M. FLANAGAN, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, WESTERN UNION; AND NEAL J. ROBINSON, EXECUTIVE VICE PRESIDENT, U.S. TELEPHONE COMMUNICATIONS, INC.

Mr. ROBINSON. I am Mr. Robinson, executive vice president and chief financial officer of U.S. Telephone.

Mr. BROPHY. Theodore Brophy, chairman and chief executive officer of GTE Corp.

Mr. BROWN. C. L. Brown, chairman of the board, American Telephone & Telegraph.

Mr. FLANAGAN. Robert M. Flanagan, chairman of the board and chief executive officer, Western Union.

Mr. McGOWAN. William C. McGowan, chairman of the board, MCI Telecommunications Corp.

Chairman DINGELL. Gentlemen, it was the practice of the joint committee meeting yesterday that each of our witnesses would testify for 5 minutes and that the entirety of the record of each of our witnesses would be inserted in the record. This is because of the very large number of witnesses to be heard from and because of the very large number of members from both committees present for this hearing. So each of you gentlemen will have your statements inserted into the record in their entirety, and we will recognize you for 5 minutes each.

Gentlemen, starting if you please with Mr. Brown.

Mr. BROWN. Thank you, Mr. Chairman and Senator Packwood. I am here to answer any questions you have, but I would like to respond to the concern expressed by Senator Packwood in his letter to his Senate colleagues. As he stated, the concern we are dealing with is for the universal telephone network. This is the overall network which permits nearly everyone in the country to reach nearly everyone else quickly and inexpensively.

I would submit the whole is what is important, not just the individual parts. Since the 1960's we have tried to point out the price shift effects of the introduction of competition into a monopoly rate structure. These effects were disbelieved or ignored until recently. Now the pendulum seems to have swung to the other extreme and the rhetoric reflects a near panic over the affordability of telephone service itself.

Since the 1960's the debates have taken place in courts and regulatory chambers and in Congress itself about the structure of the Bell System and its effect on the national desire for competition. We got the message and we agreed to drastically change the structure to comply with what we read as public policy. The last time I sat here the concern was for the viability of the Bell operating companies. That concern seems to have calmed as we worked out the divestiture plan over the last 19 months.

Now with 5 months remaining before divestiture, concern over local rates has become the issue. It is largely voiced by State regulators who have nearly full control over these rates. Legislative proposals are now on the table which would attempt to turn back the clock and restore an economically irrational and anticompetitive pricing system. Public policy is for competition in communications, and yet we appear to be worried about it just at the time the consumers are beginning to see the benefits of it. They can buy or rent their telephones at a very low and competitive price, they have a wide variety of choices in telephone company rate plans, and they can take advantage of competitive low-priced long-distance service sold by a number of companies.

Preservation of the entire universally available nationwide telephone network is the objective of the telephone industry, and I believe also the objective of Congress and the regulators. It is the very life's blood of the Bell companies and the AT&T Co. after divestiture. As has been repeatedly stated, the price shifts made necessary by competition do not threaten this network nor access to it. Attempts to overturn what has been carefully designed to accommodate the transition to full competition will surely damage the universal network and will suffer the worst of all worlds, neither the benefits of a regulated monopoly nor the advantages of truly competitive environments.

Rate increase requests need to be kept in perspective, and an important factor which is frequently ignored is that there will be rate decreases which will occur along with them. It is really a customer's total bill with which we should all be concerned. We do not applaud all parts of the FCC access order. The latest version increases the penalty carried by AT&T. But the order has been carefully worked out by the FCC over a period of years and squarely faces the problem. The order now provides for a waiver of the resident customer access charge where it is desired to target a subsidy toward needy people. Lifeline services can assume the effect of life in most States.

I feel that at last we are progressing towards solutions to matters which have plagued this industry for decades. We will be glad to work with the Congress and the regulators to see that the effects are carefully monitored and do not damage universal service or the universal network that has made the telephone system in this country the world leader.

Thank you.

Chairman DINGELL. Thank you.

[The statement follows:]

STATEMENT OF CHARLES L. BROWN, ON BEHALF OF AMERICAN TELEPHONE AND TELEGRAPH CO.

My name is Charles L. Brown. I am Chairman of the Board of the American Telephone and Telegraph Company. I am appearing today, at your invitation, to state our views on the many bills pending before your Committees. However, the rapid pace of recent events has precluded detailed analysis of these bills. Quite apart from the fact that a number were not introduced until late last week, the FCC announced only two days ago revisions in its access charge decision of last December. We are studying these bills in the light of the FCC's revised decision, and will be pleased to provide both the House and Senate Committees with our views in detail as soon as feasible.

My testimony this morning addresses the broad public policy issue raised by these bills: how best to preserve universal telephone service in the highly competitive and rapidly evolving telecommunications market. Although my testimony focuses on the universal service concepts which underlie all of the bills, many of these pending bills deal with other subjects, such as procurement quotas, patent licensing, depreciation issues, prohibitions against deaveraging long distance rates, provision of terminal equipment by the BOCs, and other issues. Many of these other provisions are highly objectionable, some downright anti-competitive. I would like the opportunity to file written comments on these points when our analysis of them has been completed.

Preservation of universal service is a matter of grave concern to AT&T. The historic mission of the Bell System has been to promote universal service. And it is in the future business interests of both AT&T and the Bell System operating companies to preserve universal service. After all, without an access line, the customer has no use for the services and equipment we are selling. But AT&T is equally concerned that efforts to preserve universal service do not jeopardize the financial health of its to-be-divested Bell Operating Companies ("BOCs"), threaten the universal national long distance telephone network, or stifle innovation in this vital national industry.

The FCC access charge decision of last December appropriately balanced these considerations. State regulatory commissions continue to have ample authority to assure that the explosive competition that now exists in the telecommunications industry does not jeopardize universal service.

UNIVERSAL SERVICE

Although the concept of "universal telephone service" is a familiar one, it is important to reiterate what the concept does and does not embrace. Universal service means broad public access to the telephone network. The goal of maintaining universal service depends on keeping access affordable for those who would otherwise leave the network. In contrast, universal service does not require that subsidized basic telephone service be provided to those who can afford to pay its cost. Nor does it require unlimited calling at flat monthly charges within any specified geographic areas.

Rates for access to the telephone network are now at levels substantially below cost. The lines and facilities that connect subscribers to telephone switches in order to provide this access represent enormous investments and are the major costs of transmission facilities in the network. For example, today, on the average, the facilities that connect subscribers to the network cost local telephone companies about $26 per customer line per month. These costs are fixed and are incurred by the telephone company even if no calls are placed or received over that line. There is concern that some present subscribers would not be able to afford telephone service unless their rates are set well below the average $26 per month cost.

It should be equally clear that, to the extent that any customer's residential rates are maintained below the $26 per month cost of the line to the local company, other services must produce revenues that are well in excess of their costs in order to make up this shortfall from residential rates. Failures to do so would have acute significance for the divested BOCs. Over $60 billion, more than half of their assets, consist of the "non-traffic sensitive plant" that provides access to the network.

AT&T AND UNIVERSAL SERVICE

AT&T and the Bell System have devoted our entire history to achieving universal service. Because the affordability and universality of basic telephone service are critical to the health and growth of both the long distance business that AT&T will continue and the local exchange business that our stockholders will continue to own after divestiture, the impending structural reoganization of the Bell System necessarily strengthens its commitment to universal service.

When telephone service was provided as a regulated monopoly during the first seventy years of this century, there was no impediment to setting telephone rates to advance universal service goals. Rates were deliberately and openly designed to achieve this goal. All residential rates were kept very low, under close supervision by state and federal regulatory agencies. These local rates were subsidized by setting the usage-based charges for long distance service and other services at artificially high levels and through a complex system of internal subsidies. For example, nearly 40 cents out of every $1.00 collected for interstate long distance service is used to recover the cost of local access facilities. Under this system, those subscribers who make no or few long distance calls pay much less than the $26 per month average cost of access. In contrast, subscribers who make many long distance calls, in many cases, pay their individual costs of access many times over, thereby paying the access costs of other subscribers as well.

This system of internal subsidies and the Bell System's and the industry's remarkable history of innovation produced the greatest telephone system in the world. It achieved universal service, under any realistic meaning of that concept. In 1940, only 37% of households had telephones, even though it required six hours of work by the average person each month to pay monthly service. By 1980, it took less than one and-half hours of work each month to pay for the same service, and 93% of all households had telephones. If often became cheaper, as well as faster, to use the telephone than to mail a letter.

THE INTRODUCTION OF COMPETITION

Although the regulated telephone monopoly was then viewed with admiration and envy by other countries, the FCC, in the late 1960s, sought to change it. It proposed the introduction of competition into major aspects of the telecommunications industry, including long distance service. AT&T opposed these changes. We argued that they would make it more difficult to preserve universal service because artificially high above-cost long distance rates and cross-subsidies of local service simply could not be maintained in a competitive environment. Proponents of competition argued, on the other hand, that competition would promote economic efficiency precisely because it would drive prices toward costs.

After long debates in the regulatory bodies, in the Antitrust Division of the Department of Justice, in federal courts, and in the halls of Congress, we got the message: the regulated monopoly and the traditional principles on which the Bell System was built and universal service achieved were no longer desired. We also recognized that other technological changes, especially advances that blurred the line between telecommunications services and data processing, required changes in public policy. Indeed, the telecommunications industry is now characterized by such explosive competition and rapid innovation that no one can confidently predict its future development. Accordingly, we long ago stopped arguing for continuation of the regulated telephone monopoly. That ship has sailed. We adjusted to the new competitive era by agreeing to a massive structural reorganization. It is now proceeding under tight deadlines under the close supervision of Judge Greene and in accordance with applicable state and federal regulatory requirements.

Competitive conditions have forced telephone carriers to undertake the repricing of services that had been predicted in the 1970s. The system of requiring heavy users to pay "access charges" (through usage-based rates) that are many times the fixed $26 per month cost of their access lines unavoidably leaves the exchange carriers vulnerable to uneconomic bypass of the network through the burgeoning technologies that are developing. Uneconomic bypass means a customer's use of alternative services solely because of higher rates which are not justified by the economic costs of providing service. When large users leave the network, they make no contributions to the cost of maintaining the more than $60 billion investment in non-traffic sensitive plant. This cost must then be paid by fewer customers, thereby increasing the average cost per subscriber. The net effect of such bypass is thus to increase local rates and imperil universal service. By the same token, requirements that the AT&T intercity network charge artificially inflated rates leave it vulnerable to selective competition from private systems as well as those other common carriers who are required to make far lesser contributions to local service. When that occurs, those residential customers and small businesses that do not have the volume of usage to use bypass alternatives will pay higher rates for use of the common carrier network. Thus, the very customers who are the subject of the intended benefits will end up paying more for both local and long distance services.

The FCC's Access Charge decision adopts a moderate program that will gradually phase out most usage-based charges to recover the fixed access costs allocated to interstate telephone service and it phases in a system of fixed charges on the customer who causes them. The FCC Order provides for a flat monthly access charge of $2 for residential customers in 1984. To temper any potential effects on universal service, the FCC's order provides for a waiver process of the flat monthly charges for lifeline service, and adopts a mechanism to support local rates in high cost areas.

There is one essential point that has not been clearly understood. I want to emphasize that the FCC's decision does not mean that the total revenues currently received by communications companies, including the Bell System, will change. This is not a rate increase. It is a shifting of costs. Total carrier revenues may change for a variety of other reasons, such as changes in costs of doing business or changes to achieve a fair rate of return, but they will not change because of the FCC's decision on end user access charges. Under that decision, more money will be paid directly to the BOCs but less money will be paid to AT&T. The total bills of customers who make many long distance calls will go down. The bills for other customers will either stay the same or go up (but subject to the exceptions as needed to preserve universal service, discussed below). Most critically, the decision reduces uneconomic bypass and makes it far more likely that the BOC's or AT&T's services will be used when they are most efficient.

There has been considerable confusion about this decision. It is easy to find these issues confusing. But it is essential that all of us start off in this discussion from the same place with the same understanding of the facts. The facts are that total carrier revenues will not go up because of end user access charges; economic efficiency will be advanced, and universal service need not be impaired.

THE FCC DECISION DOES NOT IMPAIR UNIVERSAL SERVICE

Against this background, we believe the FCC's access charge decision of last December is moderate and balanced.

Obviously, a decision to have the end user pay the access line costs could have no adverse effect on the affordability of service for those customers whose *total* bills would go down or remain the same. By the same token, it would not drive from access to the network those customers whose bills would go up, but who can afford to make the payments. Nor would the decision unfairly affect any affluent customers who do not use the long distance network (if there are any), because those customers still impose a $26 cost to the network each month and are the most appropriate parties to bear these costs (remembering that if they don't pay their full cost, some other customer will ultimately bear that cost).

Concern about universal service should, therefore, be directed to those low-income customers who cannot afford to pay the costs of basic telephone service. The need of low income people for telephone service, like the other necessities of life—clothing, food, electricity, and shelter—can be met by public assistance payments from tax funds. But Government subsidies are not necessary for telephone service because of the availability of lifeline rates which permit the receipt of unlimited calls and a very limited number of outgoing calls for rates currently up to $6 per month. Lifeline rates are already on file with some 30 state commissions in tariffs developed with the Bell System's assistance. Because the intraexchange service that accounts for over 90 percent of all calls retains substantial natural monopoly characteristics, the States are free to make up the shortfall by imposing modest surcharges on other intraexchange services. By targeting these lifeline rates to members of low income groups who would otherwise leave the network, state commissions can minimize the economic burden on other intraexchange ratepayers—all without creating serious uneconomic incentives. The state commissions have the authority to create a variety of targeted intraexchange service options and packages that can protect universal service without additional legislation.

THE PROPOSED ALTERNATIVES WOULD BE COUNTERPRODUCTIVE, HARMFUL, AND INEFFECTIVE

The alternative to the FCC's access charge decision that has been proposed is to retain the existing system of usage-based charges to cover fixed costs, but to guard against bypass by attempting to charge for bypass, or even to prohibit bypass altogether. Although these proposals have theoretical appeal, we strongly doubt that they could be effectively administered or enforced. Moreover, they threaten a vital national resource: the only universal network that exists.

Critics of the FCC's decision recognize the reality that the existing system for recovery of fixed access line costs leaves the BOCs vulnerable to bypass. Thus, they are searching for an alternative mechanism that would prevent bypass, either altogether or at least when it is economically inefficient.

One proposal is to require bypassers to contribute to local telephone service as if they had used exchange access services. This is essentially a tax on bypass. We question how this could be administered because there is no formula or method of which we are aware that could be used to develop "equivalent charges." For example, how are charges to be measured when a commercial printer or newspaper transmits the text of a book by satellite from a rooftop in Chicago to one in New York? Are voice equivalent charges to be used? Are special data charges to be developed? More fundamentally, how can the charges be developed for the hybrid new technologies? It is no answer to hand off the problem to the FCC in the absence of standards that can be rationally administered.

We also question whether making bypass a crime is likely to be effective. Bypass is not only very difficult to detect, but with the development of hybrid new technologies, bypass could occur even where the bypassers genuinely intended to conform to the law. In sum, we do not think these proposals could effectively protect the BOCs and their ratepayers.

These bills would create very large subsidy requirements which would in the end be passed on to every long distance customer, whether collected by AT&T or some other carrier. Before creating a system of subsidies which has these adverse effects, it is important to ask who will pay, who will receive, how much in total will be needed and what the real cost will be in terms of economic efficiency. And it is important to distinguish a limited subsidy, such as the high-cost area fund adopted by the FCC and as to which broadening the base of contributors is desirable, from the very different proposal in pending bills that would abolish the FCC-prescribed end user charges and attempt to recover that amount from interexchange carriers and private systems.

EFFECT OF THE UNIVERSAL NATIONAL NETWORK

Some of the proposals would imperil the interexchange network which can provide service to every point in the United States. Because the network is vital to the national economy and to the national defense, the efforts to protect the intraexchange user and network will be misguided in the extreme if their effect is to destroy our only national network.

Some of the pending bills would prevent interexchange carriers from reducing rates to cost and thus preventing them from effectively competing with private systems—even when they are the low cost provider of service. Both the national interest in preserving the universal network and basic equity require that such artificial constraints on AT&T be eliminated.

In sum, it would be unwise to attempt to continue the system of recovering fixed customer access line costs through usage sensitive charges. In a system of competitive long distance telecommunications services, long distance rates can no longer subsidize local rates in this fashion. Lifeline rates administered by the States are the answer to the concerns about preservation of universal service that we all share.

We recognize that the Communications Act of 1934 is in need of modernization, and the Committees' interest in this matter is reflected in various provisions of the bills that have been introduced. The respective statutory jurisdictions of the federal and state agencies warrants particular study to accommodate the 1934 Act to current conditions. And, with the increasing intensity of competition, especially in the intercity communications and equipment markets, the 1934 Act needs revision to reduce regulation where it is no longer necessary or appropriate, and to do so in a way that provides for full and fair competition by all participants on equal terms.

We look forward to working with the Committees and their staffs in studying needed amendments to the 1934 Act.

I thank the Committees for inviting me. I will be pleased to answer any questions you may have.

Chairman **Dingell**. Our next panel member is Mr. Brophy. Thank you for being with us.

Mr. **Brophy**. Mr. Chairman and Senator Packwood, I appreciate the opportunity to appear before this joint hearing. We at GTE share common objectives with the Congress: One to make available to all the people of the United States efficient telecommunications service at reasonable rates; two, to promote competition and to reduce regulation in the provision of interexchange telecommunication service, and three, to assure the continued economic health of local exchange carriers which serve our critical public and national defense needs.

As you have recognized, our industry is undergoing sweeping changes. If not made with care, these changes could undermine the common objectives we all seek. The present concerns stem in large part from the fact that interexchange revenues have been increasingly used to subsidize local telephone service. With the breakup of the Bell System on January 1, 1984, the current process through which $10.7 billion of subsidy flows from interexchange service to local service will effectively terminate. Anticipating the problem, the FCC has been seeking possible solutions for 5 years. It issued a modified order dealing with the problem only 2 days ago. We generally support the order. While it is not a perfect solution, there may not be one.

Clearly your two expressed concerns must be satisfied by any solution. Universal service must not be put at risk by an unmanageable increase in local rates, and a burden must not be imposed on interstate service in a manner which will cause large users to bypass the network with the resultant escalation of cost of local service.

As to your first concern, a high-cost fund appears to address the needs of the rural subscribers. The States can effectively address the needs of the impoverished consumer through a combination of a means-tested direct subsidy and the provision of lifeline service. The FCC's order appears to recognize this. A very large nonmeans-tested entitlement program subsidizing everyone is not necessary to sustain the goal of universal service.

In our search for alternative ways to achieve our common objectives, we have concluded that any replacement of the current settlement process must meet the following criteria:

One. Implementation of the new system must allow a reasonable time for telephone companies to make the administrative changes necessary to accommodate it.

Two. If not implemented on January 1, 1984, there must be an interim arrangement to replace the revenues that would be lost to the telephone companies before the implementation of the new system.

Three. A new system must be certain and unambiguous. The telephone industry cannot survive a system that is subjected to protracted litigation and challenge.

Four. A new system should not create an economic incentive for large customers to bypass the local network.

A word about bypass. I have only been able to conceive of three possible approaches to the bypass problem.

The first would prohibit the interstate transfer of information from terminating within an exchange boundary except through the local exchange carrier. I have rejected that as being politically, technologically, and economically unsound.

The second would relate to the price charged for interexchange service and the opportunity to assess interexchange service with the costs directly related to those services. Competition and market-pricing mechanisms would then determine whether the large user elected to either use bypass or use the local network. This is in essence the approach the FCC has been following and the one we generally favor.

The third would impose a tax or surcharge on those communications facilities that are not connected with the local network and utilize such revenues to subsidize local service. We have tried very hard to draft legislative language to implement this third approach, but to date we have experienced many difficulties. There are problems of equity related to those who already own facilities or where one circuit is, say, less than a mile long and another thousands of miles long or a circuit may be active or may be a standby spare;

There are problems that result from imposing a tax on a system owned by a local or State government; and there are problems of new technology which might fall outside any legislatively established definition. There are other definitional problems we ran into. If a definition is too narrow some transfers of information would escape the charge or tax, whereas if it is too broad we raise the specter of imposing a charge on computer technology. There may even be problems of unconstitutional delegation of tax power. There are many problems of uncertainty as to what the amount of revenue would be.

One thing seems clear, there is no easy solution to this complex problem. We look forward to working with the Congress to understand the issues, to identify the problems, and to find the solutions. We request an opportunity to file a supplemental comment related to the FCC's order of Wednesday.

Chairman DINGELL. That is entirely appropriate, and the Chair will receive such additional comments as each of you gentlemen and our other witnesses desire to present to the committee. Those comments will be inserted in the record at the appropriate place.

[The statement follows:]

STATEMENT OF THEODORE F. BROPHY, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, GTE CORP.

Mr. Chairman and members of the committees, I am Theodore F. Brophy, Chairman and Chief Executive Officer of GTE Corporation. GTE, through its subsidiaries, is the largest independent (non-Bell) provider of local exchange telephone service in the United States. Its domestic telephone subsidiaries serve approximately 9.3 million customers and operate in thirty-one states. GTE's Telenet subsidiary operates a nationwide public data communications network as a competitive "enhanced services" vendor. GTE Satellite Corporation is building an advanced satellite system which will be operational in 1984. GTE recently acquired GTE Sprint, the second largest non-Bell interexchange carrier and GTE Spacenet, a domestic satellite carrier. GTE also is a major manufacturer of telecommunications systems and equipment, lighting products, and precision materials.

Many of the aspects of the following statement are related to the concepts and mechanisms of the FCC Access Charge Order in Docket 78-72 adopted on December 22, 1982. I would like an opportunity to update my statement in light of the FCC's final order, adopted two days ago, in response to various petitions for clarification and reconsideration.

As a result of the development of competition in and deregulation of the telecommunications industry, there has been a need to re-examine how costs are allocated among the users of telecommunications services. We applaud Congress for focusing on this vital issue. We, as well as the FCC, have been struggling with this issue for the past five years. The FCC in its Access Charge Order took into account all of the various interests and came up with an answer which, although not perfect, is in our opinion both equitable and workable. You have shown concern about some aspects of this Access Charge Order and have proposed legislation to address those concerns. You have further recognized the need to discourage bypass by levying a fee on all bypassers. GTE recognizes that legislation which prevents costs from being shifted to local end users and at the same time requires a fee from all bypassers is another way to allocate costs among telecommunications users. The problems, as I will outline later, is that a fee on bypassers to subsidize the local exchange network may not be a practicable or sustainable solution. Nevertheless, I would like the opportunity to continue to work with you to determine reasonable alternatives which are workable.

I. CURRENT ENVIRONMENT

During the past two decades a dramatically altered environment has been evolving in the U.S. telecommunications industry. Indeed, even the boundaries of telecommunications and other sectors of the economy are being blurred through interactions of the marketplace and technology. For six to seven years, GTE and others in the industry have been working with Congress in an effort to develop a revised communications policy which is appropriate for our future environment.

In this telecommunications policy review, one of our fundamental objectives is to preserve the universal availability of reasonably priced, quality service. That often-expressed goal of having universal availability of basic telephone service is a common objective of the public, the Congress, and the telephone companies.[1] In the last decade other expressed objectives have evolved—competition and deregulation—so that market factors can work to give the benefits of new technology to the public at lower prices.

II. HISTORICAL BACKGROUND FOR ACCESS CHARGES

We all recognize that local telephone rates during the last several decades have not reflected the actual cost of providing the service.[2] With the concurrence of state and Federal regulators, long-distance rates generally have been set by AT&T Long Lines at much higher levels than the actual costs of providing long-distance service. On the other hand, local telephone companies have been able to sustain local exchange rates well below cost because they received subsidies from long-distance calling. Such subsidies to local telephone companies represent a substantial portion of the revenue requirement for long-distance service. This arrangement, carried out with the full understanding and support of regulators, Congress and the courts, helped to serve the important social goal of making available basic telephone service at reasonable charges to over 90 percent of all U.S. households. That goal has been essentially achieved.[3]

For a number of years, the local telephone companies and AT&T Long Lines joined to provide end-to-end service throughout the nation on a "partnership" sharing-of-the-risks basis. Through the settlements and division of revenue process, the partnership was able to subsidize the local telephone companies, both Bell and Independent. Now this partnership between the local telephone comapanies and AT&T Long Lines is being dramatically altered. The Modified Final Judgment (MFJ) between the Justice Department and AT&T mandated a breakup of AT&T and an end to the settlements and division of revenue process. The advent of competition from companies such as GTE Sprint and MCI, and regulatory actions of the FCC and the State commissions have irreversibly changed the evironment which existed in the past and make it more difficult, if not impossible, to continue the partnership. As a result, all local exchange carriers—both Bell and Independent—must find new means of collecting the revenues currently received through the settlements process.

III. FCC'S ACCESS CHARGE ORDER

The FCC's access charge proceeding, Docket 78-72, was intended to provide a new means for collecting these revenues, which would be equitable and viable in the evolving competitive environment. We believe that the Commission's December 22 Order is equitable and, just as important, workable.

The FCC has spent several years examining various methods of pricing and collecting revenues to compensate exchange carriers for the costs incurred in originating and terminating interexchange services. In particular, the FCC has been concerned about the proper method of recovering exchange carrier costs which do not vary with the amount of usage—the nontraffic-sensitive (NTS) costs allocated to interstate services. It is important to emphasize that these NTS costs are costs that would be incurred even if there were no connection to an interexchange carrier network.

In general there are two potential sources of revenue to repay NTS costs. The first are the long-distance carriers who use their local exchange connections to terminate their calls. The second are the end users of the local exchange connections on whose behalf the investment has been made.

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[1] Universal Service was mandated by Section 1 of the Communications Act of 1934, which states as a fundamental goal of FCC regulation "to make available, so far as possible, to all the people of the United States a rapid, efficient, Nation-wide . . . wire . . . communication service . . . with adequate facilities at reasonable charges." This goal has been substantially achieved, with more than 90 percent of all U.S. households receiving telephone service today, at rates which are quite affordable.

[2] Long-distance service have not always contributed to covering exchange carrier nontraffic-sensitive costs. Up until 1947 all local NTS costs were paid directly by customers in local rates. Since 1947 ever greater proportions of NTS costs have been allocated to the interstate jurisdiction. The underlying basis for this trend since 1947 is the decreasing costs of interexchange facilities and the increasing costs of exchange facilities.

[3] Over 90 percent of the United States households equates to 77 telephones per 100 people in the United States. This compares to 40.3 per 100 for the Federal Republic of Germany, 45.8 per 100 for Japan, 44.6 per 100 for the United Kingdom, and 7.9 per 100 for the Soviet Union.

The FCC in its Access Charge Order required that the part of the NTS costs of a customer's network connection which is allocated to interstate jurisdiction be recovered through two types of payments called "access charges": flat rate charges to the end user for each local exchange access line,[4] and usage-based charges all interexchange carriers for their traffic originated and terminated through the exchange network.

In addition, the Access Charge Order would impose on AT&T a so-called "premium access" charge to reflect the fact that its access to the local exchange network is technically superior to that currently afforded the other interexchange carriers such as GTE Sprint.

It is GTE's position that the Commission's Access Charge Order is sound in principle. GTE has, however, pointed out to the Commission the inadequacy of the "premium access" charge, and has challenged the Commission's extension of carrier-type access charges to a single class of noncarriers—the enhanced service providers. On the other hand, GTE agrees with the Commission that it is appropriate to impose a modest fixed monthly charge upon every telephone subscriber, to reflect the value of the subscriber of the capability to access, and to be accessed by, all interexchange carriers. It should be noted that the NTS investment for a subscriber who elects to make no interstate calls is no less than for a subscriber who makes many such calls.

V. PRESENT CONGRESSIONAL CONCERNS

All of the many telecommunications bills introduced recently in the Senate and House have addressed the FCC Access Charge Order as well as certain other areas with which we have some concern.

(1) *Elimination of end user charges.*—The first of our concerns would be any elimination of the direct "end user" charge provided for in the FCC's Access Charge Order.[5] The bills, I believe, recognize that to eliminate end user NTS charges and to place the entire NTS cost recovery burden upon users of interexchange services and private interexchange systems represents a subsidy of local telephone service, at the expense of the long-distance user. A general subsidy of all local exchange service—through removal of any "end user" NTS charges—would provide a subsidy where no need has been demonstrated. In effect, such a subsidy is equivalent to a "non-means tested" entitlement program. Further, continued reliance on interexchange user charges to recover NTS costs represents a real threat to exchange carriers, through bypass of their facilities by major communications users to avoid paying the interexchange user charges.

Local exchange service at current prices is one of the American consumer's great bargains. The average monthly charge for basic local service nationwide is on the order of $10–$11, and has increased only 77 percent over the last decade, a period during which the Consumer Price Index has increased by 131 percent and the average household income has increased by 111 percent. Even with end user access charges provided for in the FCC Order, the average telephone bill will still remain a good buy.

The opponents of end user access charges claim that, even at the modest levels established by the Commission, a number of local telephone subscribers will discontinue their service, and that the principle of "universal service" will thereby be destroyed. We cannot agree that these charges would have such an effect. However, for those few customers who could possibly be affected by an end user charge, a direct governmental subsidy to provide a lifeline service to low-income subscribers would be preferable rather than a subsidy to all end users on a non-means tested basis. Individual states have the capability to direct the offering of a means-tested lifeline service. In fact, the FCC Access Charge Order has waiver provisions which would allow lifeline services to escape payment of flat-rate end user charges.[6]

It is important to realize that access charges themselves are not rate increases; they are merely a restructuring of the method of collecting the same amount of money currently collected. Instead of collecting this money only from interstate long-distance users, the FCC order provides that the same aggregate revenues will gradually be collected from all subscribers of the local network. Similar intrastate proposals are pending before State commissions. Thus, to the extent access charges are applied, those users who make few long-distance calls will see an increase in their bills—while others who make many long-distance calls will see their total bills decrease. In other words, the total pool of local and long-distance revenues remains the same.

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[4] The FCC also gave the exchange carriers the option of substituting for a portion of these falt-rate charges a usage-based charge related to the subscriber's volume of interexchange calling.

[5] The Order mandated a minimum charge of $2 per residence line per month and a business charge of $4 per line per month.

[6] See FCC Third Report and Order, CC Docket No. 78-72, ¶¶136 and 137.

Much of the recent concern with universal service has stemmed from the unprecedentedly high rate increase applications currently pending before the State commissions. Contrary to several articles in the press, these state rate applications are not the result of the FCC's Access Charge Order.[7]

(2) *Bypass.*—Bypass of local telephone facilities by interexchange carriers and private telecommunications users is a current and growing reality. A vast array of technological alternatives is available today, and those alternatives are growing in variety and reducing in cost.

The bills now before the Senate and the House recognize that the continued recovery of NTS costs through interexchange user fees will dramatically increase economic incentives to bypass the local exchange network. When bypass occurs on a large scale by the handful of users who make the majority of business interexchange calls,[8] then it would leave the local exchange carriers with all of the NTS costs to be covered by the remaining low-volume, high-cost users. This situation will inevitably lead to continually higher local end user rates with only the most marginal users remaining.

Therefore, the bills prescribe various mechanisms directed at barring or reducing bypass.

There are three basic ways of addressing this bypass issue: preclusion of all bypass; assessment of charges on bypassers whether or not they use the public network; and shifting of NTS costs to the end user.

If bypass could be prohibited, which we doubt is possible, it would discourage technological innovations by long-distance carriers and would eliminate the incentive for technological innovations by exchange carriers—the combination of which would inevitably lead to a decline in the U.S. telecommunications capability. In addition, any bypass prohibition would probably not be politically acceptable if applied to certain end users such as federal, state and local governments. If Congress were to grant exceptions, it would inevitably have to come to grips with the difficult question of where to draw the line.

The second alternative is to assess a charge or fee on bypass facilities whether or not there is connection, directly or indirectly, to the public network. Since the charge, to be sustainable, must be assessed on users as well as nonusers, it is doubtful that a "user fee", rather than a tax, could be employed. Therefore, Congress would have to levy a braodly based tax on all interstate information transfers and to use this source of revenue to keep exchange rates lower.

There are several critical questions that need to be answered before such legislation is enacted. They are:

A. Which type of entities are taxes? These would need to include municipal, state and federal government systems; all telecommunications and nontelecommunications public utilities, except exchange common carriers; all domestic and international record carriers; all CATV companies; radio common carriers; and satellite carriers, to name but a few. It is sound from a social veiwpoint to assess such a tax on all such entities? Which one should be excluded? Should some entities who already have their own private telecommunications network facilities be grandfathered? If so, does that create an inequity in the tax? Let me give you a specific example. Railroads and pipelines have their own internal private communications network using their own rights of way. Should such entities, if they elect not to interconnect with the local exchange network, be subject to such a tax, or should they be grandfathered?

B. What is the assessment basis for such a tax? There are a multitude of possible bases on which to assess such a tax: capacity; investment; usage; value of information traversing the medium; spectrum used; revenues generated; costs incurred, etc.

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[7] The $1.7 billion increase recently filed by Southwestern Bell with the Texas Public Utility Commission is a good example. As a result of divestiture, the company expects to lose 77 percent, or $830 million, of its intrastate toll revenue. Total intrastate revenues are expected to decline 44 percent as a result of divestiture and intrastate investment and expenses are expected to decline 11 percent and 17 percent, respectively. This disproportionate impact between revenues, investment and expenses resulting from divestiture is clearly a large cause of the rate increase proposed to be recovered from local customers. None of the $1.7 billion requested increase can be directly attributed to the FCC's Access Charge Order.

[8] Seven percent of businesses generate approximately 59 percent of GTE telephone companies' total business revenue.

Each has its own value and shortcomings as a basis for assessing taxes. Whichever basis is chosen, however, will cause technological adaptions to take place, as affected entities seek to avoid all or part of such tax.

C. Who is the taxing entity? Today, telephone companies directly charge users for usage of their network. An assessment of charges for nonusage brings new administrative problems. Under the FCC Access Charge Order, an Exchange Carrier Association (ECA) will be formed to handle premium payments from AT&T, mandatory tariff pooling payments from interexchange carriers, and payments for the Universal Service Fund. The ECA Board of Directors will be named by the exchange carriers and exchange carrier personnel, on temporary assignments of two to three years, will perform ECA administrative duties. From the perpective of the telephone companies, we want to handle the charging and disbursement of funds within the industry in an ECA-type organization. However, in order to assess charges on nonusers, an excise tax rather than a fee would have to be employed. Therefore, an ECA-type private organization could not be used. The Government would be required to collect and distribute this tax, which would put the Government in the middle of the telecommunications industry. Is this a sound approach? Will it lead to greatly expanded regulation?

D. Who is taxed? Any charge must be applied to all bypass facilities used for interexchange telecommunications. Telecommunications is a term which is not easily defined, as the FCC discovered in attempting to implement its Computer I decision. A narrow definition of "telecommunications" would allow other forms of information transfer to escape any payments, thereby stimulating further technological adaptations to escape the taxable definition. Under this scenario the impact of bypass would be felt by exchange carriers.

The third alternative is the approach taken by the FCC in its Access Charge Order, that is, the eventual shifting of the NTS costs to the end user over a transition period. This method does not guarantee that bypass will not occur, but it allows the local exchange carriers to offer their facilities to interexchange carriers on the same economic basis as other local facilities.

In summary, imposing a bypass prohibition may, to begin with, not be feasible—but if it is, it would discourage technological innovations by both the interexchange and exchange carriers. Furthermore, it may not be politically desirable to impose such a prohibition on all users. If bypass is discouraged, rather than prohibited, by payment of a fee or tax, you have to deal with a new set of questions. From the foregoing discussion of the questions raised by imposing such a tax, you can readily see the complexity. With complexity comes uncertainty. When a capital-intensive business faces uncertainty, the capability to raise capital is hampered. If we have uncertainty for a long period of time, the continued difficulty in raising capital would lead to an adverse effect on the quality of service for all exchange customers. GTE will be investing $3 billion per year over the next five years in exchange facilities and equipment. To do that, we cannot have great uncertainty in our sources of revenues.

If, on the other hand, Congress does not prohibit or economically discourage bypass through assessment of charges and at the same time provides that all interstate NTS costs be picked up by the interexchange carriers, the exchange carriers will inevitably lose their major users and be forced to increase their local rates to the remaining customers.

(3) *Universal Service Fund.*—The various bills would create a Universal Service Fund for the purpose of subsidizing high-cost local exchange services, with charges to be levied upon both interexchange carriers and noncarrier entities connecting interexchange facilities or services directly or indirectly to the local exchange carrier. The particularized subsidy of the high-cost local exchanges is needed. The FCC has, in our view, already taken major steps to establish an appropriate Universal Service Fund. A danger in the creation of a Universal Service Fund is to peg the threshold level so low that there is subsidy for even those customers who are just slightly above average costs. Inevitably, to have an average there must be those above as well as those below the average. Furthermore, low threshold levels and coverage of most or all costs above the threshold leads to encouragement of inefficient exchange carrier operations.

(4) *Capital recovery.*—The legislative history of the Communication Act of 1934 shows that Congress intended to preempt State commission jurisdiction over depreciation rates for carriers subject to FCC jurisdiction. Congress felt that the setting of depreciation rates by the FCC is essential because it has substantial effects on the interstate telephone network.

Several of the bills recently introduced contain language which would, for the first time, transfer jurisdiction over depreciation rates for intrastate plant from the

FCC to the State Commissions. This would pose grave problems for the telephone industry, for its consumers, and for the nation as a whole.

The FCC has, since 1980, taken several courageous steps to recognize that the traditional regulatory practices as to depreciation and capital recovery, established in an era of little or no competition, are not appropriate for today's conditions of widespread competition and rapid technological obsolescence. The FCC, by its capital recovery actions, has started the process whereby the financial viability of the telephone companies, in time, will be assured, enabling them to continue to provide excellent service, and to use equipment which is technologically "state of the art."

The FCC's capital recovery actions have not, unfortunately, been followed by certain states. These states are in effect borrowing from the future, so that tomorrow's customers will pay for today's capital consumption.

Borrowing from the future may look good in the short run, but in the long run it is self-defeating. The higher costs to the ratepayer which follow from a higher rate base will overwhelm the initial benefits of lower depreciation expenses. Excessive dependence on high-cost external capital further drives up costs. Budget constraints caused by inadequate internal funds generation lead to deferred modernization, low productivity, and reduced service quality.

Capital recovery is a long-term issue affecting the viability of the nation's telecommunications infrastructure. If the U.S. is to remain economically and technologically competitive in world markets, fundamental policies directly affecting the very fabric of this national infrastructure must be made on a national basis from a responsible, long-term perspective. The FCC has shown the vision and fortitude to do this. Unfortunately, some of the states have not.

(5) *CPE issues.*—Several, but not all, of the bills address issues which are CPE related:

A. The exchange carriers would continue to be obligated to provide, on a regulated basis, a single one-line telephone set and associated wiring. This proposal would be contrary to the AT&T Modified Final Judgment (FMJ) and the FCC's Computer Inquiry II and would cause considerable confusion among the exchange carriers who are currently implementing this court order and the FCC decision. Moreover, since CPE is available today at reasonable rates from many different suppliers, including mail-order houses, there does not seem to be a need to require the exchange carriers to provide such a service.

B. Two bills require that an exchange carrier, through a separate subsidiary, may only offer new, deregulated terminal equipment to the public after January 1, 1984, if the equipment is manufactured by unaffiliated persons. This prohibition is not needed because:

(i) Terms and conditions under which exchange carriers procure equipment from affiliated manufacturers are normally considered during state rate hearings, effectively precluding cross-subsidization.

(ii) Existing antitrust laws also act as a deterrent against abuses of the type implied in the proposed legislation.

(iii) Finally, there has not been a need demonstrated for this extraordinary provision whereby Independent telephone companies providing new deregulated CPE in competition with the numerous other CPE suppliers would be restricted from obtaining any of this new CPE from affiliated manufacturers.

(6) *Vacation of the FCC access charge order.*—Finally, some of the bills would vacate the FCC's Access Charge Order. However, in my opinion simply overturning the Order does not offer a workable solution.

The essence of the FCC Access Charge Order is to define access-related local distribution costs and the method of recovering such costs in connection with the interexchange use of local distribution facilities. Further, the Access Charge Order defines the relationship between exchange carriers and interexchange carriers.

If Congress were to pass a law which overturns the entire FCC Access Charge Order, the following problems would be created:

A. There would be no common basis for defining the access costs of exchange carriers;

B. Without Part 69 of the FCC Rules, there would be no basis on which to define exchange and interexchange costs in a manner that coincides with the geographic demarcation of the LATAs and Associated Independent Territories; and

C. Future business relationships between exchange and interexchange carriers in view of the MFJ and the GTE Consent Decree would be negotiated between the carriers with no specific federal guidelines, which would mean that all interexchange carriers, including AT&T, would be free to negotiate with exchange carriers to obtain the best price. It is doubtful that existing access revenue flows could be maintained by an exchange carrier in such an environment.

A second implication is the encouragement of potential bypass installations in the near term. Since with a simple vacation of the Order, there would be no indication of future rules, conditions and rate levels for access charges, many entities would proceed to construct bypass facilities in such a period of uncertainty. Once these bypass facilities were in place, they would continue to be used even after a new access charge structure was eventually implemented.

In Summary, merely vacating the FCC's order would create a void, with an exchange carrier's fixed costs made more vulnerable in the absence of rules, and encourages the construction of uneconomic bypass facilities in the interim.

V. MORATORIUM ON IMPLEMENTATION OF FCC ACCESS CHARGE ORDER

Many in Congress are expressing concern about the implementation on January 1, 1984 of the FCC's Access Charge Order, and suggest that an eighteen-month delay in the effective date of the FCC Order would allow Congress more time to reflect on these issues.

Such a delay could be used to create an alternative NTS cost recovery mechanism which responds to the Congressional concerns without imposing unworkable conditions on the industry. Although I do not recommed this approach, I would like to share with you some of the principal provisions which must, in our opinion, be included in any legislative approach in order to implement such a postponement.

1. The AT&T divestiture of the BOCs would take place as scheduled, on January 1, 1984.
2. The charges to AT&T, by the BOCs and other telephone companies, for exchange access, would be based on a tariff or settlements process which would recover the dollar amounts resulting from the present separations methods.
3. ENFIA rates would continue for the other common carriers. Resellers and other entities would compensate local exchange carriers for connections on the present basis.
4. Exchange carrier revenue requirements for interexchange costs and exchange access costs would be equal to the return authorized in the Commission's 1981 Order *In re AT&T*, 86 F.C.C. 2d 221.
5. Part 69 of the FCC Rules, established by the FCC's Access Charge Order, would remain in effect for purposes of identifying interexchange costs and exchange access costs for both interstate and intrastate traffic.
6. The existing separations process, including frozen SPF, would have to continue at least for the postponement period.
7. In spite of my previous comments relative to the inability and inadvisability of attempts to preclude bypass, some means must be found to at least discourage AT&T from bypassing local exchange carriers during the moratorium period, to prevent irreversible harm.
8. The provisions of the FCC's Joint Board Docket, 80-286, and Access Charge Docket, 78-72, on High Cost Factor and Universal Service Fund, would have to go into effect on July 1, 1985.
9. The legislation would have to provide that the antitrust laws would not be violated even though the settlement's procedure is permitted to continue.

CONCLUSION

I have outlined for you several concerns I have as to the many bills on telecommunications now being considered by Congress. I am confident you will give these concerns adequate consideration. In our opinion the FCC's balanced solutions do not necessitate legislative action at this time.

It is most unfortunate that the divestitue of the BOC's and the costs associated with it occur at the same time as the initial implementation of the FCC Access Charge Order. As I have pointed out, most of the recent BOC rate increase requests are directly attributable to the divestiture and to other factors such as changes in depreciation rates, not to the FCC Access Charge Order.

Since Congress has indicated a strong interest in reviewing the implications of the currernt environment, as I mentioned earlier, we would like the opportunity to continue to work with you to determine reasonable alternatives which are workable. In addition, we would like an opportunity to return to Congress with recommendations after we have had an opportunity to study the FCC's recent actions with regard to this matter.

Chairman DINGELL. Our next witness is William G. McGowan.

Mr. McGOWAN. Thank you, Mr. Chairman. I want to say at the outset that MCI understands and shares the concerns about increases in local rates. That does not mean, however, that we believe that hasty congressional action is necessary. In fact, the legislation under consideration here today, S. 1660 and H.R. 3621, would do nothing about the majority of pending intrastate rate increase requests which now total an estimated $7.5 billion. Instead, these bills would raise total charges for all customers, adversely impact competition in both the long-distance and local distribution markets, impede the development of new technologies, and encourage inefficiency on the part of local telephone companies. MCI believes that if local rate increases threaten the widespread availability of residential telephone service—which is by no means certain—then the solution should be a program that targets subsidies directly to those in need.

Let us look at some facts.

In State after State, local telephone companies are blaming competition and divestiture for local rate increases. This is a smokescreen designed to obscure the fact that the bulk of the requested increases are for higher rates of return, faster depreciation, and—as you well know—a substantial amount that they put on top to compensate for what will be disallowed by the commission. Furthermore, these companies intend to load most of these revenue requirements on local telephone service. Some companies are actually proposing to reduce intrastate long distance rates, despite the fact that they will be left with the highest-cost toll plant, putting a further burden on local rates.

If higher profit margins and faster depreciation are justified at all, then certainly they affect a company's entire operations and should be allocated accordingly. In any case, these rate cases should not have been filed now. Instead, they should wait until after divestiture when the various commissions and the operating companies themselves have actual experience operating in the new environment. Nonetheless, telephone companies are using the uncertainty generated by the restructuring of the industry in an attempt to force monopoly ratepayers, local telephone users, into picking up an increased share of total revenue requirements while positioning themselves for anticipated intrastate competition.

In Texas, Southwestern Bell requested a $1.2 billion rate increase (exclusive of $500 million in carrier access charges) of which $910 million is for increased earnings, costs, and capital recovery. Pennsylvania Bell is asking for $315 million in local rate increases while seeking at the same time to reduce long distance by $56 million or almost 20 percent of what it proposes to increase local rates by. Ohio Bell proposes to reduce its long distance rates by 40 percent. Pacific Telephone proposes to reduce its long distance rates by $72 million. Not coincidentally, competitive carriers either do provide or are seeking to provide intrastate services in each of these States.

What we can see from these examples is that State commissioners have ample authority to deny unjustified or anticompetitive changes, to redirect any revenue requirements that are justified, and thereby alleviate the impact on local ratepayers. Why assume now that State commissions will not exercise that authority? State commissions have historically granted only 25 to 40 percent of requested increases on average.

The Congress should not proceed now on the basis of fundamentally incorrect assumptions. There is no evidence that local telephone rates must increase dramatically. The telephone industry will be a $90 billion industry in 1984, and the FCC's access charge decision will affect approximately 4 percent of that in additional customer charges. There is therefore no need to impose a new system whereby local telephone companies are subsidized by the long distance calls that people make. We believe that this would be unsound public policy for several reasons.

More than 55 percent of long distance calling is residential. It certainly is going to be unpopular to follow local rate increases with overcharges on long distance.

People would be required to pay, regardless of ability, so as to subsidize others, regardless of need.

Perverse incentives for greater inefficiency would be established.

The most efficient part of the industry would be taxed to support the least efficient—denying consumers the benefits of competition.

Private systems and new local distribution services would effectively be discouraged, if not prohibited, stifling innovation and also putting a burden on taxpayers as Federal, State, and local governments are major users of such systems.

As a practical matter, information technology is at a point where you cannot differentiate between what is local and what is long distance, making any distinction between the two meaningless. In addition, digital transmission technology makes it impossible to know whether it is voice, data, or video that is being transmitted.

America, which has demonstrated technological leadership in data processing, is about to do the same in telecommunications and information services. Do not let this Congress be the Congress that stopped America from asserting world leadership in these vital disciplines.

MCI believes that the Congress should wait until the AT&T divestiture is accomplished and the FCC's system of access charges is implemented to determine what—if any—support for local rates is necessary.

If the Congress determines then that support is required, it should be targeted for those individuals truly in need. A system could be established, for instance, which would mandate lifeline rates for certain defined groups and paid for by a telephone company's other profitable services. H.R. 3647, introduced by Representatives Markey and Luken, is one good example of this targeted approach which also addresses other critical issues such as FCC jurisdiction over all interexchange services. S. 1667, introduced by Senator Lautenberg, is another example of an approach that should be studied.

In conclusion, MCI urges the Congress to carefully consider the necessity for action now and the adverse impact that legislative proposals would have on competition and innovation in this industry.

We are opposed to the legislation we are discussing today. If this bill had been passed 10 years ago, the United States would not have a domestic satellite industry, would not have value-added carriers, would not have specialized carriers, would not have a competitive equipment industry, would not have the possibility of cellular radio, digital pagers, the possibility of DTS, MDS, probably not have fiber optics, single sideband radio or digital radio, would not have subcarrier transmission, would not have a distributed data processing industry, or centralized reservation systems.

Thank you.

Chairman DINGELL. We thank you very much for your testimony. We apologize to you for having to adhere to this 5-minute rule.

Our next panel member is Mr. Robert M. Flanagan, chairman of the board and chief executive officer of Western Union. Thank you for being with us.

Mr. FLANAGAN. Mr. Chairman, Senator Packwood, and members of the committee. Thank you for the chance to speak today and to comment on this proposed legislation. These bills are intended to permit the public to enjoy the benefits of this Nation's evolving telecommunications capability while still protecting the goal of a telephone service that everyone can afford, and they are trying to do this at a time when substantial increases in local telephone rates are pending right across the country, increases which are often tied to the implementation next January 1 of the FCC's access charges decision.

In fact, the access charge decision is not the only force behind these local increases. Some of the other factors at work include more rapid depreciation, deregulation of customer-provided equipment, perceived losses in interstate toll subsidies, increases in operating costs, and an alleged need for higher rates of return.

Thus, legislation which is directed exclusively at the access charge issue will only address part of the problem of rising local rates. At the same time there is a very real danger that these bills will place penalties on nontelephone services, penalties that may cripple a variety of existing communication services on which many of this Nation's businesses depend.

For example, Western Union's telex service makes no use whatsoever of the switched telephone network but would be taxed anyway in order to subsidize local telephone rates. I must say to you today that it is an absolute injustice to impose a tax on a service such as telex, which doesn't access the switched network, which is a source of record communication services for thousands of small businesses and which from both a historical and an economic standpoint is entirely unrelated to the local telephone service you wish to support.

In addition, some of the provisions of these bills could stifle the development of the communications technologies that are needed for the construction of future communications highways through our economy, which brings us to the threat of bypass. Bypass of the Nation's telephone system is not new and it is questionable whether it is undesirable.

Congress itself, in the Post Roads Act of 1866, authorized Western Union to construct and operate the first bypass system a decade before Alexander Graham Bell. We have been providing communication users with alternate distribution systems ever since, and the nationwide phone system seems to have survived very nicely.

Coming to today, I believe that one clear national advantage of divestiture is that Western Electric is free at last to export communications products, with all that means for our trade balance, for employment, for inflation. The drift of this legislation in its bypass provisions faces the other way.

Banning bypass or taxing it is like ordering the tide not to rise. It will happen anyway, but other countries will get the benefit in services, in exports, in jobs. That is what this legislation threatens to do. It is our belief that this and other anomalies in these bills are a result of the pressure-cooker atmosphere in which you are trying to address this dilemma.

While we applaud your willingness to address the complex problems before us, the time remaining before divestiture is just too short to address in specific substantive terms these issues.

We fear that any attempt to enact legislation under this time pressure is likely to result in unanticipated and perhaps irreversible adverse effects on the telecommunications network.

Let me give you some numbers. On October 3 the Bell System intends to file approximately 90,000 pages of tariff material describing to the FCC and the rest of us the enormous increase in access charges due to go into effect 90 days later. Those 90,000 pages are more than three times the volume the FCC processes in a normal year.

Either we are serious about the regulatory process or it is a facade. If we are serious, we should admit that the FCC cannot process 3 years' workload in 90 days. If we are not serious, let's admit that, instruct AT&T to forget the 90,000 pages of paperwork, make its filing next week so the rest of us will have an extra 60 days to decide what prices to raise and what services to eliminate or to introduce. Or maybe we should all admit that January 1 is just too near for what we are trying to do here.

Western Union is not saying that this Congress should not act. However, we submit the wisest course at the time is to give the concerned parties time to do it right. We do not say delay divestiture. Instead, we seek an orderly transition after divestiture. That is the most likely way to achieve reasonable local telephone rates without stifling the development of competitive services.

Therefore, we believe Congress should enact simple legislation which does four things: Postpone the implementation of access charges for 2 years until January 1, 1986, and extend the existing division of revenues and settlement arrangement. Convene a joint board to look at the matter, require that when tariffs are filed there is adequate time to deal with it, and finally, continue the present interim arrangements until January 1, 1986, in order, if you will, to bypass the need for new access planning in the interim.

Legislation of this sort would give the FCC and Congress time to develop hard information on the likely impact and to deal with it properly.

We are at a watershed for this country's communications networks. The rational and measured approach we advocate seems to us to offer the best prospect for achieving the right result for the American public. That concludes my remarks. Thank you.

Chairman DINGELL. Thank you very much.

[The statement follows:]

STATEMENT OF ROBERT M. FLANAGAN, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, WESTERN UNION CORP.

Mr. Chairman and members of the committee, my name is Robert M. Flanagan and I am Chairman and Chief Executive Officer, of the Western Union Corp. I am grateful for the opportunity to appear at this hearing and to give my views on proposed legislation that, if adopted, will have a profound impact on the telecommunications industry for the remainder of this century and beyond. Given the vital role that this industry plays in our nation's economy and society general, I do not think it overstates the case to say that the telecommunications issues now before Congress represent some of the most significant issues on the domestic policy agenda at this time. The fact that you have decided to conduct joint hearings on these bills certainly attests to the importance you attach to these matters, and I share with you that conviction.

Your action in convening joint hearings also reflects a recognition that prompt action is required if a more orderly transition into the post-divestiture world is to be in place before January 1, 1984 when the FCC's access charge plan is due to take effect. It is my firm belief that if Congress does nothing else but establish an adequate moratorium to provide the designated regulatory bodies and itself with the time needed to sort out the true effects of divestiture, deregulation, and termination of the existing division of revenues and settlements process, it will have taken a major step toward assuring the continued availability of affordable universal telephone service without sacrificing the technological and economic benefits that will be derived from a fully competitive telecommunications industry.

The issues before Congress are not simple, and their solutions will have profound consequences. By their express terms, the bills before you are intended to permit the public to enjoy the enormous and far-reaching benefits of this nation's sophisticated telecommunications capability without affecting the universality of basic telephone service itself. To preserve these benefits, competition must be allowed to grow and prosper. To ensure universal local exchange access, prices for telephone service must be affordable. These two principles—competition and universal service—are well accepted by Congress, the courts and the Commission, and each warrants concern. However, at the present time there is a perceived tension between them. Any resolution of that tension must not sacrifice either princple, for the costs to the public of doing so would be inestimably severe.

The transition from a monopoly environment to a competitive market is the source of many of the changes whose effects are of concern to you today. The elimination of the traditional division of revenues and settlements process, and its replacement by a system of access charges, is one component of that transition. This change, as I am sure you are aware, has contributed to the unprecedented rate increases being sought by the Bell Operating Companies from state utility commissions. These increases, however, are also the result of several other factors. A brief review of these factors will put these pending increases in proper perspective and assist you in identifying the actions required to achieve the two goals of universal service and competitive markets.

The first of these factors is the FCC's decision to grant increased depreciation rates for the Bell System. The FCC's action has resulted in increased revenue requirements which the local carriers are attempting to recoup in their recent rate filings. The issue of depreciation is obviously a concern of Congress and I am pleased to see that it has been at least partially addressed in H.R. 3621.

Another factor affecting local rates is the FCC's deregulation of customer premises equipment (CPE) in the Second Computer Inquiry. This decision requires the transfer of existing or embedded CPE to the separate non-regulated arm of AT&T (i.e., American Bell or ABI). According to tariff filings made in several states, the revenue derived from the provision of this equipment has generally exceeded the associated cost and the excess profits have been used to subsidize local rates. Before these contentions can be accepted, however, significant factual questions must be answered. Are the Bell Operating Companies transferring the proper costs to ABI along with the CPE? To the extent the BOCs will contine to maintain such equipment, are their charges to ABI adequate for the performance of that function? A thorough examination of the facts is clearly warranted.

Another factor related to local rate increases is the cessation of intrastate interLATA toll operations by Bell local exchange companies as required by the Modified Final Judgment in the antitrust litigation. Some have alleged that a subsidy runs from toll service to local exchange service and that the termination of that subsidy will necessitate rate increases by the local companies. Even assuming arguendo that there is a subsidy, an obvious question is where will the excess revenues go? Is the newly established AT&T inter-LATA carrier going to receive a windfall? If so, can these funds be identified or will they be swallowed up by AT&T's new competitive efforts? Congress and the state commissions need time to ascertain the answers to these questions.

Finally, the local Bell companies are requesting higher rates to offset increased operating costs and to provide higher rates of return that are alleged to be needed in the post-divestiture world. While state regulatory commissions traditionally address these matters, the rash of claims and counterclaims concerning divestiture and access charges, makes it impossible for the states to piece out whether the proposed rate increases are reasonable in the short time remaining before the FCC's access charge plan takes effect.

I have raised these factors, Mr. Chairman, because I think it is absolutely critical that any attempt to protect universal service be initiated with a complete understanding of the complexity of the task. This complexity is compounded by the clear and imminent danger to the development of competition that some protective measures may impose. Competition and universal service are not incompatible policies. Indeed, the full power of the Information Age will never be realized unless and until both goals are achieved.

I am particularly concerned that an attempt to solve this multifaceted issue by addressing only access charges is unilkely to succeed, and as a result, unnecessary restrictions on competition will be imposed. These shackles will hobble not only companies offering telecommunications services, but the millions of customers who directly and indirectly benefit from the availability and efficiency of alternative competitive services. Therefore, I believe that it is essential that careful study and analysis underlie any action taken in this field. This is particularly true when significant risk is involved in the manner in which otherwise commendable policies are implemented.

I am also concerned with the ability of the regulatory process, both State and Federal, to deal effectively with the mass of tariff material which is expected to reach mammoth proportions by October 1983. According to the FCC's 1983 report to Congress, the Bell System Companies access tariff filings alone are expected to result in 32,000 pages of cost support material and 65,000 pages of tariff material, all of which are to be filed on October 3, 1983, to be effective January 1, 1984. This compares with the approximately 24,000 pages of tariff material which is currently received annually from all other tariff filings. This does not take into account the tariffs to be filed by AT&T Long Lines which are expected to contain a restructuring of virtually all of its rates, nor does it reflect the access charge tariffs to be filed by independent telephone companies. The FCC will have only 90 days to review these tariffs and the supporting documents. Interested parties, including Western Union, will have only 25 days to analyze these materials, assess their impact, and file whatever protests may be necessary with the Commission.

Thus, the FCC will be required to process possibly three times as many tariffs in the last quarter of 1983 as it normally processes in an entire year. The affected parties will be deprived of any meaningful review of these tariffs. Since all tariffs, absent appropriate legislation, will have to be in place by January 1, 1984, the FCC may have no alternative but to rubber-stamp the filings.

Similarly, state commissions are being pressured to approve massive rate increases by January 1, 1984, under the threat that failure to do so will impair the ability of the local carriers to provide service. In such circumstances, the public may be required to pay excessive telephone rates and long distance competitors of AT&T may be subjected to anticompetitive charges. In short, the lack of adequate time for the FCC and state commissions to consider these tariffs could result in a complete breakdown of the regulatory process, leaving the public and competing carriers subject to excessive and predatory rates and charges.

Turning now to the merits of the legislation before you, I want to stress that Western Union shares your desire to achieve the twin objectives of universal service and an efficient and competitive telecommunications system. The goal of maintaining affordable telephone service is clearly laudable. Our sense of equity and our social conscience require that a service as essential as the telephone is made available, at least for emergency use, to all who desire it.

While your concern with the threat of substantially increased charges for local exchange service is certaintly justified, I wish to emphasize that it can only partially be attributed to the FCC's access charge decision, and thus will only be partially ameliorated by legislation addressed solely to that issue. As I outlined above, in significant respects the pending state rate filings that have recently made headline news because of their unprecedented size are the result of circumstances that are not solely attributable to the FCC's access charge plan.

This brings me now to the second objective of the proposed legislation—promoting economic efficiency and technological and service innovation. Unfortunately, I fear that certain provisions of the proposed bills will frustrate rather than enhance these goals. In fact, they may thwart economic and technological incentives. Moreover, for the first time, they will place substantial handicaps on telecommunications services which have never been viewed as a source of subsidy for basic telephone service.

Western Union's situation presents a good example of how the proposed legislation can have a seriously adverse impact on existing telecommunications service offerings. For decades, Western Union has been offering Telex/TWX services which are, essentially, an outgrowth of basic public telegram service. These hard copy message services make use in many locations of dedicated, non-switched, Bell System local distribution facilities. In other locations, local distribution is provided over Western Union's own facilities. In no instance do these services directly or indirectly access the switched telephone network. Further, because they do not access the switched network, they have never been part of the division of revenue and settlements process, and, as a result, they have never been viewed as a source of support for local telephone service.

In both the Senate and House bills under consideration by your committees, Telex/TWX and other services that have never made use of the local switched network or provided a subsidy to local telephone service, may now be indiscriminately lumped together with services that do access the switched network and have always been part of the subsidy process. As a result, these dedicated services could be saddled with burdensome charges that bear no relation to the cost of providing these services or, for that matter, to any rational plan for keeping basic telephone rates at affordable levels.

My concern with the proposed legislation goes far beyond the desire to avoid the economic distortions that are introduced into the marketplace by the imposition of a non-cost based "tax" placed on facilities and services that have been in existence for decades. Particularly in the case of Telex/TWX services, the cost burdens imposed by the bills raise serious questions as to whether Western Union can continue to offer these services on an economically viable basis. In short, the inclusion of Telex/TWX services as a source of support for basic telephone service threatens to deprive thousands of small businesses of the only record telecommunications service that they can afford. I therefore implore you to remove from the reach of the bills those services, such as Telex and TWX, that do not access the switched network, and which are, from both a historical and economic standpoint, totally irrelevant to the issue of supporting the costs of local telephone service.

I would like to think that the inclusion in the proposed legislation of dedicated, non-switched services that do not access the switched network, was merely an oversight. Unfortunately, the structure of the bills, in particular H.R. 3621, suggests otherwise. It appears that the bills reflect a concern—which I believe is unjustified—with the potential for bypass of the telephone system. As a result of this concern, all persons who employ alternatives to switched network distribution in any way and for any (commercial) purpose may be required to pay local exchange carriers for the costs of plant that they will never use.

This draconian response ignores the fact that "bypass" is simply competition. Let me assure you, "bypass" is not a dirty word or a loathsome disease. Nor is it a new phenomenon. Western Union has owned and operated local distribution facilities for over a century, even before the telephone was invented. No one has ever charged that these facilities threatened universal service objectives, or has ever advocated that they should bear a burdensome tax in order to protect local telephone companies. Western Union's distribution facilities have co-existed with local telephone plant in the streets of this nation's cities without ever causing an increase in local telephone rates.

By removing all economic incentives to employ alternative distribution facilities and, indeed, by penalizing the use of such facilities, not only will the development of alternative technologies be severely deterred, but there will be significantly less reason for local telephone companies to meet the increasingly sophisticated telecommunications needs of its customers. The needs are rapidly outpacing the local carriers' ability and/or desire to provide necessary facilities. If they go unmet, the economic growth that is expected to be spurred by tomorrow's advanced telecommunication network will be seriously impeded.

A good case in point is Teleport, a project involving Western Union, the Port Authority of New York and New Jersey, Merrill Lynch, and the City of New York. When completed in 1986, Teleport will offer a high capacity local distribution system for access to high-technology satellite communications services in the New York City area. To meet the demanding requirements of Teleport's potential users for ultra-high speed data transmission, graphics, computer-aided design, video conferencing and other specialized services, Western Union is installing a state-of-the-art fiber optic system to provide distribution from the satellite earth station's location.

Teleport has been attacked by Bell System representatives and others with parochial interests as a threat to local telephone service. However, a careful look belies these contentions. In an area plagued by local transmission bottlenecks, Teleport is an important alternative to either forcing businesses to relocate to less crowded regions or requiring them to abandon their plans for business expansion that depends on highly sophisticated telecommunications services.

If Teleport or similar distribution systems are made economically obsolete by protectionist legislation, the results could be devastating. Areas that have insufficient or outdated local transmission plant such as New York City, which is already experiencing a business exodus, could be faced with the loss of thousands of jobs and millions of dollars in tax revenues. Businesses which require the type of innovative facilities that the local telephone companies cannot deliver on a timely basis will simply move elsewhere or forego their expansion plans.

Since the local exchange is the technological weak link in the interstate telecommunications network, removing a competitive spur to increased performance in this market reduces the efficiency of the entire network. It does customers little good to have the most sophisticated computers communicating over high capacity interexchange lines if the last mile brings the whole service down to "tin can" quality levels. The all-encompassing subsidy scheme contemplated in the proposed legislation, if allowed to take effect, is sure to thwart any incentive for technological and service innovation in local distribution systems and could relegate this nation to second-class status in the information age.

I wish to emphasize that this is not a doomsday scenario, but rather a realistic forecast of the likely outcome of legislation that apparently was conceived without an appreciation of all relevant information. The next several decades will rely on telecommunications as the driving economic force. Congress must take extra care not to establish mechanisms that inhibit the full development of our telecommunications capability. It must also make certain that the best possible environment for full and fair competition exists so that all suppliers of telecommunications products and services, including the local exchange companies, are encouraged and motivated to innovate and utilize technology that offers the best promise for low cost, high quality services to the public.

In sum, Western Union applauds the willingness of Congress to address the difficult and complex problems that confront all users of our telecommunications network today. However, given the limited time remaining before divestiture is implemented on January 1, 1984, I fear that any attempt to deal in specific substantive terms with these very complex issues, entails a substantial risk that any such legislation, no matter how well intentioned, will result in unanticipated adverse effects on this nation's telecommunications industry. In my testimony today I have illustrated two situations in which the bills now before you could very seriously impair the provision of needed telecommunications services to the public. Furthermore, the proposed legislation's focus on the issue of access charges will, as I have discussed, leave untouched many other cost factors that underlie the rate increases which are now pending before the states.

As I see it, the core problem is the limited time that is available to deal with these issues between now and the scheduled divestiture date of January 1, 1984. It is the January 1 date which is the driving force behind the FCC's rush to implement its new system of access charges; it is the January 1 date which gives rise to the tremendous pressure on state regulatory commissions to approve the local telephone rate increases that are pending before them; and it is the same January 1 date which has compelled Congress to take action as well.

I submit that the wisest course of action to take at this time is to give all concerned governmental parties—the Congress, the FCC, and the state commissions—more time to analyze the issues that confront them and gauge the effect on the public of the solutions they propose. I do not seek any delay in the divestiture of the Bell System. Rather, what I seek is an orderly transition, following divestiture, to ensure the establishment of reasonable rates for local telephone service and for access to interstate service.

To this end, I propose that Congress enact legislation containing the following specific elements:

1. The requirement of the MFJ that the BOC's file access charge tariffs to replace the division of revenues and settlements process effective January 1, 1984, should be postponed until January 1, 1986, and that process should be continued during the

interim period. In order to permit continuation of the present contribution of toll revenues to support local exchange services, the bill should provide that AT&T shall be entitled to no more than its costs (including its rate of return as prescribed for interstate servcies by the FCC). The balance of these revenues should be remitted to the appropriate local exchange carrier.

2. A Joint Board should be convened to consider the effect of the FCC's proposed access charges on the goal of universal service and to make recommended changes as necessary. These recommendations, and comments by interested parties thereon, should serve as the bases for a new system of access charge rules to be promulgated by the FCC.

3. Tariffs to implement the new access charge plan should be filed no later than March 31, 1985. This will give the Commission at least nine months to scrutinize the access charge tariffs and prescribe any necessary replacement tariffs, or take other appropriate action, prior to January 1, 1986. The deferral of the effective date of the access charge tariffs above will also permit the state commissions to adopt similar procedures.

4. The ENFIA tariffs, now marked to expire April 15, 1984, should be extended through December 31, 1985, in order to provide a statutory basis for the payment of compensation by the OCC's for their use of local exchange services and facilities. The bill should provide, however, that the telephone operating companies may adjust the rates and charges in these tariffs in accordance with the provision of the ENFIA agreement. These adjustments include those to reflect increases in operating costs as well as increases in utilization of access lines by the OCC's.

Legislation containing the provisions I have outlined above will have several beneficial effects. It will give the FCC and the Congress time to develop additional information concerning the likely impact of the Commission's access charge plan on the goal of universally-affordable local telephone service and will permit the FCC or the Congress, if necessary, to take appropriate action to modify this plan. It will also give the Commission additional time to evaluate the reasonableness of the access tariffs that are filed by the various telephone companies, and will establish the framework for competitive telecommunications services that the FCC, the Congress, the Court, and the parties to the antirtrust settlement all envision for the future. By continuing the existing division of revenues and settlements process my proposal wil obviate the need for immediate increases in local telephone rates to offset the revenues that the local companies would otherwise have lost. Thus, the state commissions will no longer be "under the gun" to see to it that the local companies' revenues are increased before the end of this year and they will have much-needed additional time to consider and analyze the complex rate proposals that are now pending before them.

In closing, I note that H. Res. 231, submitted by Mr. Wyden and Mr. Swift and reported unanimously on June 29 by the House Subcommittee on Telecommunications, indicates concerns identical to those I have expressed and recommends a procedure similar to that contained in my legislative proposal. In addition, the letter of July 20, signed by Mr. Luken, Mr. Markey and six others members to their colleagues on the Committee also expresses the same concerns.

Western Union will be happy to assist your committees in drafting legislation that we believe would accomplish the goals discussed above.

Chairman Dingell. The last panel member is Mr. Neal J. Robinson, executive vice president, U.S. Telephone Communications. We understand Mr. Devlin, who was to be with us today, is not feeling well. We hope that he is returned to full health.

Mr. Robinson. Thank you, Mr. Chairman.

We fully support the preservation of universal telephone service. We share the concerns of Congress in the need to maintain local telephone service at reasonable, affordable rates. We believe an appropriate system of charges for exchange access can alleviate a significant portion of the upward pressure of local telephone rates while solving a problem of critical importance to long-distance telecommunications companies which compete with AT&T.

This approach is compatible with the direction taken on Wednesday by the FCC on reconsideration of its access charge decision. Approximately 400 companies compete in providing long-distance telecommunications service. This competition has been a direct result of SEC and court decisions establishing a clear public policy in favor of increased competition.

This competition has provided great efficiency in the industry, expanded utilization of existing facilities and lower long-distance telephone charges to the consumer. Notwithstanding the beneficial competition which characterizes the long-distance telecommunications industry, local exchange facilities remain monopolies without access to local exchange facilities controlled by these monopolies, no competitive long-distance telephone company could survive.

Currently under an arrangement known as ENFIA, Exchange Network Facilities for Interchange Access, the long-distance competitors of AT&T pay for access to local exchanges. AT&T divides revenues with its local operating subsidies pursuant to a procedure known as division of revenue. By means of these payments, long-distance telephone revenues have historically contributed to the revenue requirements of local exchanges, helping to control local telephone rates.

Of course, with the 96-percent share of the long-distance revenue market, the bulk of this revenue comes from AT&T, and to a substantial extent it is the fear of the potential loss of this revenue that has precipitated the recent spate of unprecedented and largely unjustified local rate increase filings by numerous local operating companies, rate increase filings unrelated to competition, the actions of FCC or divestiture.

By assuring a continuation of the present system of access charges, H.R. 3621 may alleviate much of the need for new local revenues and provide a basis for State utility commissions to reject this unwarranted mass of rate increase filings. Under ENFIA there is a difference between the amount paid by AT&T for access to the local exchange and the amount paid by competing long-distance competitors of AT&T.

Although both AT&T and competing interexchange carriers receive local exchange access, the access AT&T receives is far superior to that provided competing long-distance companies. For instance, the quality of voice communication is better, with far less noise and static. Telephone users wishing to place a long-distance call through the AT&T system need dial only 10 or 11 digits. Customers of AT&T's competitors must dial as many as 24 digits.

Due to the superior nature of its interconnection, AT&T can serve customers with rotary dial phones. AT&T's competitors cannot, unless their customers incur additional costs.

In addition, AT&T receives superior billing information than that provided by AT&T competition, including identification of the calling customer's account number and confirmation of the successful completion of a call. The higher access charges paid by AT&T simply reflect the superior quality of the interconnection provided to AT&T. As a result of its superior connection to the local exchange, AT&T receives a level of service that competing long-distance companies do not receive and for which they do not pay. The superior interconnection enjoyed by AT&T results in benefits and competitive advantages to AT&T and competitive disadvantages to the competing companies.

In many cases the value to AT&T of its superior interconnection is far greater than any added cost of the local exchange of providing this interconnection. Conversely, competing long-distance companies incur substantial additional costs in attempting to reduce the deficiencies of inferior exchange access. These costs far exceed any savings experienced by a local exchange in providing an inferior interconnection for AT&T's competitors. So long as equivalent access to the local exchange remains unavailable to long-distance competitors of AT&T, the existing differential on access charges cannot be eliminated without undermining the viability of competition in long-distance telecommunications. H.R. 3621 largely incorporates this principle.

A deficiency of the House bill shared by the Senate bill is the absence of an assurance that equivalent access to equivalent means of interconnection will in fact be provided to competing interexchange carriers as equal exchange access charges are substituted for the current system. While we are optimistic that equivalent means of interconnection will be provided by local operating companies following divestiture, prudence dictates that we recognize the potential for delays in attaining this objective.

As a practical matter it is likely to be some time after the dates prescribed by the FCC and the district court before equivalent access is actually provided in many exchange areas. By proceeding cautiously through a gradual substitution of a new system of access charges, a more orderly transition to a post-divestiture communications industry will be assured. As previously indicated, reduction of uncertainty respecting the full level of local operating company revenues will alleviate the pressure on local telephone rates.

Thank you very much.

Chairman DINGELL. The Chair thanks the members of our panel.

The Chair announces that under the rules laid down yesterday, the two committees will recognize members in the order of their appearance, and not only the most timely, but the distinguished chairman of our sister committee, the Senator from Oregon, Mr. Packwood, is recognized first.

Chairman PACKWOOD. Mr. Chairman, are we also working on a limited-time rule so that we will each ask questions for a set period of time and go back through another round?

Chairman DINGELL. Yes. Each member will be recognized for 5 minutes in turn and we will go through the members as often as is required to get the necessary number of answers.

The distinguished Senator from Oregon is recognized for 5 minutes.

Chairman PACKWOOD. Mr. Brown, let me address this to you. In both lobbying on this bill and in testimony yesterday the Bell operating companies, perhaps to a lesser extent AT&T, have used the argument with some legislators that their States are going to lose money, that more money will flow out of their State than will flow into the State. Is that not simply, and indeed it is true, but is that not a function of how much long distance is placed from each State and where the long-distance centers are, and indeed big towns, the New Yorks, Chicagos, Los Angeleses, probably initiate great numbers of long-distance calls, and this will be used to subsidize residential rates in other States?

Mr. BROWN. I think it reflects more the cost—it is the high-cost factor which is involved here in the FCC's order. Those States which are compact and have a telephone plant which was put in at lower prices over the years would be feeding money to States which have new plant which is put in at higher prices and therefore more costly. I believe it is more a function of the age of the plant and the compactness of the northeastern areas, and California.

Chairman PACKWOOD. That accounts more for the money flowing into the States than it does flowing out, does it not? The outflow is being generated by the long-distance calls?

Mr. BROWN. That is correct.

Chairman PACKWOOD. In theory does that differ from the corporate profits tax, where the argument is used that we generate more money than we receive from this tax? It is true that the major corporations of America for years are located in a relatively few States and they generate more money into the corporate profits tax?

Mr. BROWN. Yes. I had not thought of the relevance of that comparison.

Chairman PACKWOOD. Put the other way around, we faced this problem on the gasoline tax last year, and Texas gravely complained that more money is raised in the gasoline tax than is spent there. The money flows out of Texas and many of the Western States because we drive more, into the compact Eastern States where highway construction is incredibly expensive; that the money is flowing into those States from States in the West where the highways are done and where the construction costs are not nearly so great and yet the revenue produced is greater proportionately than in the compact States?

Mr. BROWN. Yes. I think the concern is for the customers of these States, in some of the aging Eastern and Northern States. The concern is why should those customers, as individuals, making long-distance calls, subsidize places like Florida. It does not seem reasonable——

Chairman PACKWOOD. Why should the drivers in Oregon subsidize completion of the Westway in New York?

Mr. BROWN. I do not really know why they should, and I imagine you do not think they should.

Chairman PACKWOOD. There are questions above and beyond financing. As a matter of fact, I have supported it. Of course the example used most frequently is the windfall profits tax. I doubt if much of it is collected in Massachusetts, although my hunch is a fair portion of it may be spent in Massachusetts. I only ask these questions for this point. If we are talking about a national social policy of universal service, and we can disagree whether the bill introduced by Chairman Dingell and Chairman Wirth and myself is the right policy or not. But if we are talking about a national policy, is it a valid argument to say we will attempt to constrict it intrastate, or an argument against the policy is that more money might be raised in some State and spent in another?

Mr. BROWN. No. I think it is worthwhile to bring up the effects of what is happening so it is clear to Senators what is happening. If it is decided that that should be happening, so be it.

Chairman PACKWOOD. So as long as we are able to raise it under all circumstances and money flows both ways. Yesterday there was much reference to the Perl report and whether or not it was accurate. I think it was the public utility commissioner from Florida who indicated that the report was not very different from its first to its second report, the second report simply zeroed in on the access charge and therefore his figures were somewhat lower. But the report was cited as having been offered by AT&T in evidence in the divestiture case. Is that right?

Mr. BROWN. Yes, sir. I think the first report was offered in the court.

Chairman PACKWOOD. And that report apparently proved that for each 10-percent increase in rates there would be about a 1-percent loss of customers?

Mr. BROWN. I really cannot recall what the first report indicated. I understand the second report, which reflected Perl's understanding of current situations, indicated that for example a $2 increase might result in a 1-percent——

Chairman PACKWOOD. So one of the congressional Members, I think one of the House Members, took it to its conclusion, I think Congressman Swift, when he said, "Well, that was based upon a $2 access charge, and if you were to extend that to $7, ultimately if you had your 10-percent increase in rates would you have a 1-percent drop in customers?" He concluded yes, and apparently the report concludes yes. I want to know if that was AT&T's position in the antitrust suit? Was that a piece of evidence offered by AT&T?

Mr. BROWN. The Perl report was surely offered by AT&T in that case.

Chairman PACKWOOD. To prove the point that you would have customer dropoff for proportionate increases in rates?

Mr. BROWN. To prove that there may be customer dropoff if the rates increased disproportionately—I think it is fair to say that the FCC waiver for the needy with respect to the $2 charge just eliminates that concern because it would be the poor people who would be inclined to drop off and their problem is solved by the waiver. So I do not think the Perl report is germane with respect to what the FCC has now done.

Chairman PACKWOOD. Thank you, Mr. Chairman.

Chairman DINGELL. The Chair recognizes the gentleman from Massachusetts, Mr. Markey.

Representative MARKEY. Thank you, Mr. Chairman.

The gentleman from oil-poor Massachusetts would like to ask questions. We make it possible for the oil companies to pay the windfall profits tax.

Mr. Chairman, 11 days ago I gave up caffeine. I decided that I had had enough of that harmful stimulant that gives you cancer, makes you ill, and most worrisome to me, I am told that it accelerates baldness. In the past 11 days I have learned, however, to live without caffeine and to be better off because of the change. I have learned about the benefits of decaffeinated coffee and colas and candies.

After yesterday's hearings I could not help but think that my experience with caffeine was somehow applicable to what we are doing here, for now we are on the verge of decaffeinating our phone system, giving up much of the system's stimulants that exist in the form of unneeded and wasteful subsidy. Like caffeine, these subsidies are hard to give up. Years of established practice, of habit, have made the addiction of a subsidy to our phone system a way of life. But just as recent medical discoveries have suggested that we are better off without caffeine, recent changes in technological innovation in the telecommunications industry dictate that we should and must abandon inefficient pricing schemes. I hear some people bemoan our fate, yet this is much like the person who suggests that the problem with caffeine is a study which tells us it is harmful.

Simply put, as it is foolish to blame the studies as the reason one must give up caffeine, it is likewise foolish to blame change and progress for ruining the golden age of the national telephone system. Furthermore, today when consumers can buy a phone for less than a third of its annual rental cost or can use long distance for one-half of the normal price, it seem ludicrous to talk about the good old days of the old network.

Like the withdrawal from any dependency, our withdrawal from the phone system inefficiencies of the past may be a rocky one. We are already seeing the tremors of withdrawal throughout our system and throughout the country. But such tremors do not mean that we should go back to the old dependency. To the contrary, what is needed is some measure to smooth the transition from the old way of life to the new one and to insure that the new one works in the best interest of all consumers.

The bill which Mr. Luken and I have introduced is such a measure. It spreads out the implementation of the access-charge decision and permanently softens its burden on consumers by increasing the average business charge. It provides a limited amount of subsidy to rural areas. It seeks to improve the effectiveness of the regulatory process by increasing public participation and mandating a 5-year study of universal service and rate increase requests. It facilitates the further development of competition in the industry.

Mr. McGowan, I was pleased to hear you say kind things about H.R. 3647 in your opening statement. I am glad to see that we share similar concerns about the future of your industry and consumers all over the country. When you were before the Telecommunications Subcommittee in March you gave an excellent presentation on the inefficiency and complete lack of commonsense that lies behind subsidies that are not targeted on a need basis. You touched again on this point again today and it is one that I tried to argue for yesterday. Since you are far more articulate on this matter than I, perhaps you would be willing to share some of your rationale for this position.

Mr. McGowan. The pricing structure in our industry is, to put it kindly, very wormy. Prices are not related to costs in many instances. Money flows from one class of users to other classes, presumably from more profitable services to less profitable, but no one knows that for sure. The industry has evolved a negotiating process—unexamined in most cases by any governmental agency—whereby, through separations and settlements, manipulation of data, manipulation of investment, various costs are distorted. This industry—through the course of FCC decisions, court decisions, and, finally, the divestiture—has agreed that it will go toward cost-based pricing. I believe everyone in our industry wishes that done.

Every user who has any knowledge about our industry wishes that to be done. We have been giving wrong signals to users about what things cost. We have been distorting costs so that people have wrongfully assumed certain services are valuable to them, and I believe everyone—and I would be so bold as to say I believe AT&T and MCI—is fully in agreement that this industry should evolve into a cost-based business. This is the only economically sound approach.

Representative MARKEY. What do you think would happen if we expanded competition on interstate toll routes? Do you think the average consumer would benefit from that kind of change?

Mr. McGOWAN. I think competition wherever possible will immediately help the consumer in the United States both from an economic viewpoint as well as from a technological viewpoint. I see AT&T has introduced more technological changes in equipment, and I believe we will find that same statement true in local services if we allow competition there.

Representative MARKEY. Thank you, Mr. Chairman.

Chairman DINGELL. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Washington State, Mr. Swift.

Representative SWIFT. Thank you, Mr. Chairman.

Kind of following up on what Senator Packwood was talking about, I have seen this material that is circulating indicating who are the haves and have-nots in terms of interregional transfers, and I believe my State is one that is an exporter according to that particular map. Yet for the life of me I do not understand why somebody in Seattle should be able to make a long-distance call to Sarasota and not pay a fair amount for the cost of the Sarasota telephone system without which he would not be able to make that call.

What we are really going to need with this issue is some more information, and because most of this seems to be flowing out of the BOC's, I am wondering, Mr. Brown, if you would be able to supply the committee for the record, not this morning, with specific information on the amount of money that is presently shifted under the separations and settlements procedure, and in addition to that under the FCC joint board decision, and if possible, if you have the information, it has to be around somewhere, because people are making all these assertions on how those then compare with transfers under the proposed legislation. Could you provide that?

Mr. BROWN. We will do our best to do it in a short time. The maps that are floating around I have to say did not come from the Bell System as far as I know. There are a good many people that are concerned about this.

[The following information was subsequently received for the record:]

Present interstate separations and settlements amounts for the year 1982 are shown in Table I. They are comprised of non-traffic sensitive ("NTS") charges, that is, the portion of the fixed costs of connecting customers to the local telephone switching office which have been allocated to the interstate jurisdiction (regardless of whether the line is used for long distance calling or not). Table IA is an estimate of present interstate separations and settlements amounts for 1984. Note that these amounts do not include other costs included in interstate separations and settlements—such as local switching and trunking, interexchange plant and dedicated facilities—which are costs directly attributable to long distance services.

TABLE I.—PRESENT INTERSTATE SEPARATIONS AND SETTLEMENTS TELEPHONE INDUSTRY, YEAR 1982

[Dollar amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷B)
Alabama	$121	$128	0.95
Alaska	40	23	1.74
Arizona	214	150	1.43
Arkansas	100	81	1.24
California	1,142	862	1.33
Colorado	240	213	1.13
Connecticut	151	205	.74
Delaware	30	43	.70
Florida	863	600	1.44
Georgia	255	266	.96
Hawaii	40	56	.71
Idaho	65	48	1.35
Illinois	431	504	.86
Indiana	183	187	.98
Iowa	106	108	.98
Kansas	119	105	1.13
Kentucky	99	106	.93
Louisiana	144	152	.95
Maine	45	39	1.15
Maryland	126	203	.62
Massachusetts	218	296	.74
Michigan	214	250	.86
Minnesota	155	149	1.04
Mississippi	92	82	1.12
Missouri	190	209	.91
Montana	64	38	1.68
Nebraska	84	78	1.08
Nevada	114	97	1.18
New Hampshire	68	67	1.02
New Jersey	351	548	.64
New Mexico	81	68	1.19
New York	843	848	.99
North Carolina	191	205	.93
North Dakota	38	33	1.15
Ohio	271	336	.81
Oklahoma	168	156	1.08
Oregon	155	121	1.28
Pennsylvania	300	453	.66
Puerto Rico	60	23	2.61
Rhode Island	37	49	.76
South Carolina	108	124	.87
South Dakota	37	29	1.28
Tennessee	138	184	.75
Texas	616	567	1.09
Utah	60	67	.90
Vermont	40	31	1.29
Virginia	214	262	.82
Virgin Islands	10	5	2.00
Washington	224	187	1.20
West Virginia	60	66	.91
Wisconsin	148	152	.97
Wyoming	70	43	1.63
District of Columbia	87	118	.74

TABLE I.—PRESENT INTERSTATE SEPARATIONS AND SETTLEMENTS TELEPHONE INDUSTRY, YEAR 1982—Continued

[Dollar amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷B)
Total	10,020	10,020	

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[1] NTS (nontraffic sensitive) represents only that portion allocated to interstate of costs of connecting customers to the local telephone switching office. They do not include amounts in interstate settlements for local switching and trunking, interexchange plant, and dedicated facilities.

[2] Distribution on originating minutes.

TABLE IA.—PRESENT INTERSTATE SEPARATIONS AND SETTLEMENTS, TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED)

[Dollar amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷KB)
Alabama	$157	$159	0.99
Alaska	46	29	1.59
Arizona	269	187	1.44
Arkansas	123	101	1.22
California	1,508	1,070	1.41
Colorado	290	264	1.10
Connecticut	181	254	.71
Delaware	36	54	.67
Florida	1,066	746	1.43
Georgia	313	330	.95
Hawaii	46	70	.66
Idaho	77	60	1.28
Illinois	488	626	.78
Indiana	217	232	.94
Iowa	132	134	.99
Kansas	146	131	1.11
Kentucky	128	132	.97
Louisiana	192	189	1.02
Maine	56	48	1.17
Maryland	158	252	.63
Massachusetts	265	367	.72
Michigan	264	310	.85
Minnesota	195	186	1.05
Mississippi	118	102	1.16
Missouri	238	259	.92
Montana	74	47	1.57
Nebraska	105	97	1.08
Nevada	155	121	1.28
New Hampshire	81	83	.98
New Jersey	419	681	.62
New Mexico	105	85	1.24
New York	1,020	1,053	.97
North Carolina	239	254	.94
North Dakota	49	41	1.20
Ohio	339	417	.81
Oklahoma	198	194	1.02
Oregon	197	151	1.30
Pennsylvania	369	563	.66
Puerto Rico	69	29	2.39
Rhode Island	43	61	.70
South Carolina	132	154	.86
South Dakota	47	36	1.31

TABLE IA.—PRESENT INTERSTATE SEPARATIONS AND SETTLEMENTS, TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED)—Continued

[Dollar amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷KB)
Tennessee	170	229	.74
Texas	779	705	1.10
Utah	75	83	.90
Vermont	49	38	1.29
Virginia	273	325	.84
Virgin Islands	11	6	1.83
Washington	279	233	1.20
West Virginia	75	82	.91
Wisconsin	185	189	.98
Wyoming	96	54	1.78
District of Columbia	108	147	.73
Total	12,450	12,450	

[1] NTS (nontraffic sensitive) represents only that portion allocated to interstate of costs of connecting customers to the local telephone switching office. They do not include amounts in interstate settlements for local switching and trunking, interexchange plant, and dedicated facilities.

[2] Distribution on originating minutes.

Estimated NTS interstate amounts under the FCC Access Charge plan for the year 1984 of $10.7 billion are shown in Table II. *Note* that these amounts do *not* include approximately $9 billion of carrier access charges for local switching and trunking and dedicated facilities.

Table IIA shows estimated NTS interstate amounts, at the 1984 level, assuming the transition to full end-user charges plus a Universal Service Fund were completed.

TABLE II.—FCC ACCESS CHARGE PLAN TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED)

[Dollars amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷B)
Alabama	$137	$141	0.97
Alaska	42	25	1.68
Arizona	239	151	1.58
Arkansas	104	87	1.20
California	1,270	1,060	1.20
Colorado	261	206	1.27
Connecticut	160	193	.83
Delaware	33	40	.83
Florida	894	606	1.48
Georgia	277	251	1.10
Hawaii	41	60	.68
Idaho	65	48	1.35
Illinois	421	524	.80
Indiana	180	205	.88
Iowa	112	116	.97
Kansas	126	110	1.15
Kentucky	107	122	.88
Louisiana	173	173	1.00
Maine	49	45	1.09
Maryland	142	218	.65
Massachusetts	230	301	.76
Michigan	231	312	.74
Minnesota	171	154	1.11
Mississippi	108	89	1.21

TABLE II.—FCC ACCESS CHARGE PLAN TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED)—Continued

[Dollars amounts in millions]

State	Interstate NTS [1] (A)	Customer payments [2] (B)	Ratio (A÷B)
Missouri	202	211	.96
Montana	64	40	1.60
Nebraska	87	73	1.19
Nevada	119	83	1.43
New Hampshire	71	64	1.11
New Jersey	370	537	.69
New Mexico	90	71	1.27
New York	887	906	.98
North Carolina	198	217	.91
North Dakota	42	36	1.17
Ohio	285	384	.74
Oklahoma	176	153	1.15
Oregon	164	131	1.25
Pennsylvania	313	503	.62
Puerto Rico	62	34	1.82
Rhode Island	38	51	.75
South Carolina	113	129	.88
South Dakota	40	31	1.29
Tennessee	148	189	.78
Texas	673	637	1.06
Utah	66	69	.96
Vermont	42	30	1.40
Virginia	230	270	.85
Virgin Islands	10	5	2.00
Washington	235	210	1.12
West Virginia	67	73	.92
Wisconsin	152	172	.88
Wyoming	88	42	2.10
District of Columbia	95	112	.85
Total	10,700	10,700	

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[1] NTC (nontraffic sensitive) differs from the present amounts by excluding certain central office elements. They do not include amounts in access charges for local switching and trunking ($6,000,000,000 estimated) and dedicated facilities ($3,000,000,000 estimated).
[2] Based on $2 residence and $6 business end-user charges and carrier charges distributed on originating minutes.

TABLE IIA.—FCC ACCESS CHARGE PLAN AT END OF TRANSITION TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED) [1]

[Dollars amounts in millions]

State	Interstate NTS (A)	Customer paymentsG52 (B)	Ratio (A÷B)
Alabama	$137	$105	1.30
Alaska	42	19	2.21
Arizona	239	238	1.00
Arkansas	104	70	1.49
California	1,270	1,327	.96
Colorado	261	278	.94
Connecticut	160	178	.90
Delaware	33	37	.89
Florida	894	712	1.26
Georgia	277	274	1.01
Hawaii	41	47	.87
Idaho	65	62	1.05
Illinois	421	463	.91
Indiana	180	193	.93

TABLE IIA.—FCC ACCESS CHARGE PLAN AT END OF TRANSITION TELEPHONE INDUSTRY, YEAR 1984 (ESTIMATED) [1]—Continued

[Dollars amounts in millions]

State	Interstate NTS (A)	Customer payments G52 (B)	Ratio (A÷B)
Iowa	112	119	.94
Kansas	126	124	1.02
Kentucky	107	86	1.24
Louisiana	173	127	1.36
Maine	49	52	.94
Maryland	142	161	.88
Massachusetts	230	256	.90
Michigan	231	248	.93
Minnesota	171	175	.98
Mississippi	108	64	1.69
Missouri	202	201	1.00
Montana	64	55	1.16
Nebraska	87	88	.99
Nevada	119	117	1.02
New Hampshire	71	76	.93
New Jersey	370	420	.88
New Mexico	90	87	1.03
New York	887	956	.93
North Carolina	198	208	.95
North Dakota	42	28	1.50
Ohio	285	305	.93
Oklahoma	176	179	.98
Oregon	164	169	.97
Pennsylvania	313	351	.89
Puerto Rico	62	62	1.00
Rhode Island	38	43	.88
South Carolina	113	97	1.16
South Dakota	40	34	1.18
Tennessee	148	163	.91
Texas	673	685	.98
Utah	66	70	.94
Vermont	42	40	1.05
Virginia	230	242	.95
Virgin Islands	10	6	1.67
Washington	235	239	.98
West Virginia	67	51	1.31
Wisconsin	152	142	1.07
Wyoming	88	65	1.35
District of Columbia	95	106	.90
Total	10,700	10,700	

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[1] Estimated 1984 amounts, assuming access charge plan transition were completed.

[2] Based on end-user charges covering all NTS except for universal service fund amounts, and carrier charges (i.e., USF) distributed on originating minutes.

Comparisons of these numbers with the twelve pending "universal service" bills are difficult for several reasons.

First, details of the various bills vary considerably, making direct comparisons difficult. Second, some bills, such as H.R. 3621, contain only general provisions on the large amounts of subsidies which would be required and leave the distribution of such subsidies to the discretion of a new joint board. Third, several bills overturn the FCC's Access Charge decision in whole or in part, making it more difficult to determine the basis (the components of plant and facilities) on which access charges are to be calculated.

As we continue to analyze these bills, we will provide further analysis.

Representative SWIFT. Could we nail down a short time—is a couple of weeks reasonable?

Mr. **Brown**. Yes, sir. I hedge a little bit because we have not seen the FCC order yet. We have seen press releases and Chairman Fowler's testimony.

Representative **Swift**. If we could have some of it now and others later—the settlement stuff is probably sitting around somewhere. I would appreciate that very much. I think it could be very helpful to us. Yesterday Chairman Fowler stressed the philosophical approach in the access charge that we should pay for what we use, and I will direct this to Mr. Brophy. It is not a new question. If the people in the system should pay for what they use, why should the customer who does not want long-distance service, does not want to make interstate calls, why should he have to pay an interstate access charge?

Mr. **Brophy**. Obviously a customer should not have to pay for a service they do not use. The fact is that you could not have local service without paying a substantially higher amount than you currently pay. Excluding inside wiring and the telephone instrument itself, the cost of local service, if fully paid by a customer who did not have access to interexchange service, would be about $19 a month. What has happened is that you take the full cost of local service—those things that are not traffic-sensitive and that are required just to provide local service. At the moment we then allocate most of that amount to interexchange service on a usage basis. But the fact is there will be no saving if the person elected not to use interexchange service. And so the only way a person will pay his full cost of local service is paying the full nontraffic-sensitive cost.

Representative **Swift**. It is always kind of amazing to me that no matter now we figure this out the consumer gets it in the end. I would like to ask another question of Mr. Brophy in particular. In the legislation as currently proposed, and let us assume for a moment that it is going to pass, and I know you prefer that it would not, but say it does, do we deal in that legislation adequately with a transition period to give the telephone industry an opportunity to do the things it is going to need to do in order to adjust? Do we deal with you properly vis-a-vis any antitrust laws that might have to be adjusted for that interim period?

Mr. **Brophy**. I think that during the interim period if there were going to be a stay of the FCC's order or moratorium that there are some things that would need to be done, and I try to outline those starting on page 20 of my written testimony. It cannot be a simple stay because in essence the agreements we now have are with the Bell operating companies that in turn get their flow of funds from AT&T, and with the breakup of the Bell System, that current method of settlement essentially disappears. There would have to be a replacement system for that which would achieve essentially the same result.

Representative **Swift**. So you deal with that in some specific detail in your prepared testimony?

Mr. **Brophy**. Yes.

Representative **Swift**. I do not believe there is anybody regardless of how strong they support this legislation that wants to create any unintended or unnecessary inconvenience for the telephone company. You have been buffeted around a lot during the past few years as we try to sort through this.

Mr. Brophy. I appreciate that. We are really not looking for increased income. We are trying to find a method of protecting ourselves against a drastic loss of revenue resulting from a change in the system.

Representative Swift. Thank you very much.

Thank you, Mr. Chairman.

Chairman Dingell. The time of the gentleman has expired.

The Chair recognizes the distinguished Senator from Washington, Mr. Gorton.

Senator Gorton. Thank you, Mr. Chairman.

If the FCC's access charge decision is in fact implemented, by how much do you predict that your long-distance rates will drop, either in absolute terms or in comparison with what will happen if we change the status quo?

Mr. Brown. I would rather see the words in the FCC order, which only came out Wednesday in press release form, before I am really able to understand what the effect on access charge is going to be. We surely intend to sharply decrease long-distance rates. The same order of which we speak increases the penalty on AT&T vis-a-vis the gentlemen at the table here, and I am sorry that I just cannot predict that until I understand what the actual words of the order say and to what extent that penalty really affects us. I can understand why some of the gentlemen at the table would like to have a moratorium, because they can continue the kinds of feeding at the trough which has been made possible by the ENFIA and penalty arrangements, but I have to say that to have a moratorium on what has been in progress for so long really does not face the problem. We will still be in the same situation 2 or 3 or however many years after a moratorium that we now face now, except that AT&T will continue to be more disadvantaged. I am sorry, I would like to give you a precise number. I just do not understand yet what the FCC order is going to do.

Mr. Brophy. I think Mr. Brown is the only one that can answer what the rates will be because we will be out of that with the breakup of the Bell System. Answering Congressman Swift's question I was not recommending a moratorium. I was suggesting that if Congress should determine that that was the direction in which to move, it is not a simple matter. I have outlined in my testimony the matters that need to be considered.

Mr. McGowan. I had three people attend that FCC open meeting and each briefed me, and then I read the commission's public notice. From their varying descriptions, there clearly had to be four different meetings. I have no idea what the commission. I am going to wait until the order comes out.

Senator Gorton. Mr. Brown, I can assure you that we would appreciate as precise an answer to that question as promptly as AT&T can deliver it.

Mr. Brown. We will be glad to supply that. We are anxious to let this be known also. One of the problems is that the concentration has been on increases in rates and very little if any concentration on the fact that long-distance rates will come down. What we ought to be worried about is the total bill. If I might say, Senator Gorton, that the total average bill of residence customers around the country is about $37, and well over half of that in most cases is long distance, so we are not seeing both sides of the scale here.

[The following information was subsequently received for the record:]

AT&T intends to reduce the rates for Message Telephone Service (MTS) and Wide Area Telecommunications Services (WATS) beginning in 1984 to an extent consistent with the company's earnings requirements and the financial integrity of the business.

Our preliminary estimates, based on the FCC's initial access charge order adopted on December 22, 1982 and released on February 28, 1983 (in Docket 78-72) indicated that overall domestic message service and WATS rate reductions of about 10 percent or more may be possible. However, the FCC on July 27, 1983, announced modifications of that decision and the text of its order on reconsideration has not yet been released.

Precise estimates of the amount of long distance service reductions must await the release of the Commission's latest order and further information on the access charge tariffs which will be filed by the local operating telephone companies, because access charges will be such a large proportion of AT&T's long distance service costs.

Senator GORTON. A question for Mr. Robinson, and if others wish to comment on it, it is certainly appropriate. If under the terms of Senator Packwood's proposal, or the chairman of the House committee's proposal each long distance carrier were required to pay a similar access or bypass charge, how could this be considered either to be anticompetitive or a disincentive to innovation? Would it not simply have a great tendency to create a level playing field in which competition would be most vigorous?

Mr. ROBINSON. Well, I would address that as follows. We certainly support a level playing field. We certainly support that the same game that goes on on the playing field is the same game that we are in. We have to recognize that we are not all starting from an equal place.

I would like to address the comment about feeding at the trough to answer your question if I may. In order to use our system, one is required to dial 23 or 24 digits versus the 10 or 11 digits that one is required to access in the Bell System. That is a tremendous inconvenience. The only way it can be overcome is with a substantial investment in capital. We cannot serve the rotary phone market. That is a market which approximates 55 percent of the telephones in this country. We have an inferior interconnection on the switch for local access. That causes hiss, hums, static, and so forth, which is frequently blamed on the low quality of the carrier's transmission. We make adjustments to our customers because of the inferior quality of the interconnection with which we are provided.

So yes, we do favor a level playing field. We would like that level playing field as quickly as possible. That is what equal access is about. We hope that equal access will be implemented on schedule. We are optimistic that it will be, but we have to recognize that it may be in fact delayed. To the extent that we do not receive equal access, we do not wish to pay for it. We would like to pay for the same things in the same fashion that the AT&T system gets.

Mr. McGOWAN. I would like to endorse that statement.

Mr. BROPHY. I probably am the only one here wearing two hats, having recently acquired GT Sprint, and I agree with Mr. Robinson on his statement. I might also say that if it were possible over a period of time to impose some kind of a tax on all carriers, whether or not they connected to the network, that obviously would be one way of subsidizing local rates. The problem we are concerned about in the telephone industry side is that there do appear to be a number of very difficult legal problems that we have struggled with. Lawyers can disagree, but the one thing the industry cannot face is uncertainty in the source of its revenue, and we do hope that whatever decision is made by whatever body makes that decision, when the system is implemented, we will have some assurance that we will be receiving the revenue that is designated for us and will not spend all of our time for the next 10 years in the courts looking for it.

Senator **GORTON**. Thank you, Mr. Chairman.

Chairman **DINGELL**. The time of the gentleman has expired.

The Chair now recognizes Mr. Wyden.

Representative **WYDEN**. Thank you very much, Mr. Chairman. It is a pleasure to be here. I have been sitting now for 2 days and it seems to me that the issue has become pretty simple, and that is that—it was clear yesterday and I think it is becoming clearer today, that everybody in this country wants universal service, but nobody wants to do very much to pay for it. Yesterday with the local telephone companies we had very conflicting messages. They said, for example, that it was logical to charge a flat rate for access to the long-distance lines, whether or not you make any calls at all, while at the same time setting up a local system that charges for every single call.

Today we have heard from you gentlemen a position I think that reflects the same kind of inconsistency. You said you supported universal service, which I think is commendable, but I do not see how in the world that the access charge decision that you have said you support is going to help us sustain universal service. I think that is in the interest of all of your companies. The question I will have for you is what are you going to do to pay your fair share to keep universal service in this country?

Let me start with you, Mr. Brown.

Mr. **BROWN**. Mr. Wyden, I guess I have been heard to say before this whole thing was not my idea.

Representative **WYDEN**. I think none of us would claim credit for it at this point.

Mr. **BROWN**. But the idea, that is the idea of injecting competition into a monopoly framework, carries with it inevitably the economic fact that prices will be driven toward costs or competition cannot exist. Now, having understood that by virtue of the competition in the long-distance business to date, even, it is not a question of fairness unless the whole American system of competition can be considered unfair.

Representative **WYDEN**. But we are not using a system of costs. We are forcing our consumers to pay for a service that they just do not use. My question to you is what will you do, what will you put on the line, what will you pay toward contributing to universal service in this country, because as of now you are not paying a single thing.

Mr. **BROWN**. As of now we are paying about $1.7 billion.

Representative **WYDEN**. Under the changes.

Mr. **Brown**. All I can tell you is that when you insert competition you have driven the economics in the other direction. Now, the customer who has—who makes no long-distance calls, which is a very rare customer, as Mr. Brophy says, really is getting a very low, uneconomic price for his local exchange service. What is also not very often talked about is that he has full and unlimited access to incoming calls. I do not think the premise that you state is germane to what is happening here. The customer is getting a benefit from this now, and it is a question of whether or not prices are to be driven toward costs as competition inevitably demands.

Representative **Wyden**. I think the principle of the change is pretty clear, and that is we are going to force customers in this country to pay for a service that they do not use, and we are going to see a lot of high-blown talk about efficiency and economic logic and the rest, but that is the bottom principle behind the change.

Mr. **Brown**. That is not correct.

Mr. **Brophy**. Mr. Wyden, might I answer you in this way. There are two elements of the cost of telephone service. One is a fixed cost, and that does not vary with the amount of usage of the system. That is being suggested to be assessed on a flat-rate basis. Then there is a variable cost that varies with the amount of use, and that we suggest should be charged for on the basis of amount of use. We are not suggesting that anybody should pay for service that they do not use.

Representative **Wyden**. But would you not still pay even if you did not make a single long-distance call?

Mr. **Brophy**. You would pay an amount no more than your cost of local telephone service. If you make no calls, or have no desire to receive them, then you do not need telephone service. But a system that would only permit you to receive calls or a system that would make only one call a month would be just as costly in terms of non-traffic-sensitive costs as a system where you made 100 calls or received 1,000 calls.

Representative **Wyden**. I think your logic is somewhat convoluted. I think it is pretty clear that you cannot say there is a cost system if you get charged for not making a single long-distance call.

Mr. **Brophy**. I will give you an example. If I have a washing machine I have to pay a price for that. If I wash my clothes once a week or once a month or do not wash them at all, there is still a cost and that is the kind of cost that is embedded in the telephone system. Somebody has to pay.

Mr. **McGowan**. We have a street system, even though a lot of people do not use the airlines, we still have a street system for them to get to the airlines if they want to.

Representative **Wyden**. Mr. Chairman, I ask unanimous consent for an additional question.

Chairman **Dingell**. The time of the gentleman has expired. The Chair will simply have to object. We have too many members here. I would love to let the gentleman continue, and we will recognize him at another time. We just cannot do that at this time.

The Chair recognizes the gentleman from Texas, Mr. Leland.

Representative **Leland**. Mr. Brown, there has been much recent discussion about the $1.7 billion rate increase requested of Texas consumers by Southwestern Bell. This effectively would raise the monthly rate for residential users to about $30-plus from about $10-plus, which represents about a 200-percent increase. Can you comment on that and the real concern here about the low- and moderate-income people who would be hurt very severely by this rate increase?

Mr. **Brown**. I am no poet on that Texas rate case, but I do understand that the figure you cite includes money which is charged by Southwestern Bell to the carriers, not to the customers at all, so a great deal of the money is involved right there. Second, I believe the depreciation figure is one which is still to be decided among commissions. And third, the Texas commission is not known for promptly rendering the rates that Southwestern Bell asks for, and I think a period of time will put that rate increase request in perspective.

Representative **Leland**. I understand that there might be some consensus that even if they do not get what they requested there might be some lower rate given them by the PUC, but at the same time you imply that that does not necessarily mean that the customers are going to be affected that much. I tend to disagree with that.

Mr. **Brown**. The reason I said what I did was that I believe some $500 million of that rate increase was talked about as a rate increase but really is a charge on the long-distance carriers. All of us here at the table are opposed to a charge on the customer. That is what I was referring to. It is not a rate increase on the customers at all. It is an access charge.

Representative **Leland**. I am not a sociologist, although that is what we are here in Congress. The fact of the matter is that the sociological implications dictate that minority people use long-distance calls at a greater percentage than most other people. I do not know if you know that.

Mr. **Brown**. Yes, sir, I do. I realize that and this is one of the very points that I have tried to make. The more long-distance calls that minority people make, the lower will be their total bill. And I think it would be a crime if artificial schemes were made to keep the long-distance rates high.

Representative **Leland**. Wait a minute. I know I did not understand you correctly.

Mr. **Brown**. Let me try again. Perhaps I am not making myself clear. What you said is correct, that minority people use the long-distance lines a lot more than others on the average. That is what you said, was it not?

Representative **Leland**. You see what you did to the lights? You are more powerful than I thought you were.

Mr. **Brown**. I think if I can shed light on this particular problem we will all be better off. As you state, minorities use long-distance more than the average customer. If the long-distance rates are kept artificially high, as some of these bills would suggest, minorities will therefore suffer. If the FCC order goes in as planned, the long-distance rates will come down, and the total bill therefore will come down for a very high user of long distance.

Representative **Leland**. You are suggesting that we ought to raise or keep long-distance rates down and raise residential rates, is that what you are saying? That is more desirable?

Mr. **Brown**. I am saying we ought to bring the prices where the costs are, as we have been talking here this morning. A $2 charge, for example, which is in the FCC order for a residential user who uses long-distance heavily will be clearly overweighed by rate reductions in both intrastate and interstate long-distance calling, unless those long-distance calls are kept at an artificially high price.

Representative **Leland**. The problem I have is that these increases are going to hurt—I used the example of minority people primarily because they represent a higher percentage, not necessarily in real numbers, a higher percentage of poor people. But I am concerned about universally poverty-stricken people, regardless. If we raise residential rates to any significant degree then we hurt targeted populations like senior citizens. How are we going to help them? Because as my colleague from Oregon has said over and over again, because of his particular concern about senior citizens, a senior citizen has, many times, only a telephone to communicate with his or her friends and neighbors in order to stay alive. How do we help them?

Mr. **Brown**. It seems to me there are two ways to help the situation, and surely from the standpoint of anybody who runs a telephone company or anybody who runs a long-distance business, the last thing we want to do is see people off the network. There are two ways. First the FCC provides for a waiver to the access charge for people who cannot afford it. Second, I do not think any of us see a problem in a targeted subsidy within a State for people who cannot afford telephone service at any rate. A targeted subsidy for the needy is endorsed I think by all of us, and I would hope that such targeted subsidies could be applied if necessary, but the idea of a subsidy for people who do not need one, people living in $200,000 houses subsidized by this artificial scheme, that does not seem to me to make sense.

Representative **Leland**. You suggest that the $200,000 category ought to be the floor for that consideration?

Mr. **Brown**. Well, I have not seen your house, Mr. Leland.

Chairman **Dingell**. The time of the gentleman has expired.

The Chair recognizes now Senator Lautenberg.

Senator **Lautenberg**. Thank you, Mr. Chairman.

Mr. Brown, since the comment was addressed to you, I have to respond to an observation of my esteemed colleague and chairman of the committee on which I sit in the Senate. He raised a point about the windfall profit tax. It is interesting to note that the windfall profit tax legislation included the creation of a subsidy that gave energy support based on need, not on the basis of whether a particular area of the Nation faces high energy costs. It is called the low-income energy assistance program. It was intended to address the problems of those who have the least ability to pay. So if we are going to draw analogies, we should be mindful of that aspect.

You may know, Mr. Brown, that I support targeting of a below-cost lifeline rate for people who need assistance in maintaining access to the telephone network. I think that lifeline service should be supported in every State in our Union, whether the general costs of providing service are high or low, where people of modest means would otherwise be unable to afford basic telephone service. You seem to agree that if Congress does see fit to mandate subsidies to insure universal affordable service, then that supported service should be targeted to those who need it.

Mr. BROWN. Yes, sir, I feel that way.

Senator LAUTENBERG. Let me ask a fairly simple question. We discussed briefly a moratorium on access charges I have to ask you, why the rush to impose that charge? If we were able to defer it by a year, I think it would give us a chance to thoroughly study the results of the divestiture process, and I think perhaps we would come up with something different by way of a formula. When we look at the addition of a $2 access charge, going up by $2 a year for a period of 3 years, that in some States represents an increase for a basic service of more than 20 percent. It does so in New Jersey, as you might know. In New Jersey we are very efficient. What would be the problem in a delay? I would like comments from any of you. Perhaps I should not invite comments from Bill McGowan. But what is the rush? If we hold off a year, do you see any dire consequence?

Mr. BROWN. Yes, sir, I do, and it is largely because I do not think we will know any more after a year than we know now. Second, there is nothing irreversible from the legislative standpoint if the FCC order goes in essentially as now predicted. It can always be changed. Third, the tide of bypassing is rising, not falling, and damage to the Bell operating companies and damage to all local operating companies will be extensive the longer this uneconomic or economically irrational subsidy continues to exist, and I think all telephone company people, especially these divested Bell companies, are going to be concerned, as Mr. Brophy says, with the effect on their revenues, and the uncertainty and the invitation to continue what is very rising—a very rising tide of bypass may very well be devastating if moratoriums and temporizing are applied to a problem which is very well understood.

Senator LAUTENBERG. Yes?

Mr. ROBINSON. If I may comment on that. We really do not see a requirement to rush forward with the implementation of a new system. Nothing real in terms of the basic economics has changed. Let us address the uncertainty of revenues issue. If we maintained the current system by establishing a moratorium, there would be no uncertainty of revenues, the revenues would still be there. One thing that is often missed is that there are other sources of revenue that will come into play. Mr. Brown spoke about the total bill. I believe we should consider that. We do not know how those charges will be determined. We do not know how those costs will be determined. So as we move forward in a rational way, if we can keep in place the current system of access charges guaranteeing the revenue, we can see how the situation evolves so that we can rationally determine what should be the prices of the other services, what revenues will they contribute and what will be the total bill.

Senator LAUTENBERG. What would be the cost to the American Bell System if we do not introduce the access charge in the year 1984?

Mr. BROWN. I do not know any way I can answer that. Are you talking about the Bell operating companies?

Senator LAUTENBERG. The long-distance companies, the long-distance service, because that is where the impact is going to be felt, is it not, with the introduction of the access charge? The individual subscriber is going to pick up some part of the load for accessing the network, right?

Mr. BROWN. Yes, and then we will reduce our charges for long-distance service.

Senator LAUTENBERG. I am talking about the direct impact of the $2.

Mr. BROWN. What will be the effect——

Senator LAUTENBERG. What will be the cumulative total of the $2 per line——

Mr. BROWN. What will be the effect on the Bell operating companies or AT&T?

Senator LAUTENBERG. No. What will be the sum total? Does anybody have that information, on the amount of money raised as a result of the $2 access charge?

Mr. BROWN. I am sorry. That may be available. I do not have it.

Senator LAUTENBERG. Well, please try to get that.

[The following information was subsequently received for the record:]

The $2 charge on residential customers ("end-users") under the FCC's access charge decision is estimated to total approximately $1.9 billion in 1984. The total of both the $2 residence and business line charge is estimated to be approximately $3.5 billion in 1984.

Senator LAUTENBERG. I wanted to say one thing to Bill McGowan. When you talked about my bill, I think you gave credit to the wrong person. I think you said Lugar, if I am not mistaken.

Mr. MCGOWAN. I corrected it with the stenographer.

Chairman DINGELL. The time of the distinguished Senator has expired.

The Chair recognizes my good friend and colleague, Mr. Wirth, chairman of the subcommittee and the sponsor of the bill on the House side.

Representative WIRTH. Thank you very much, Mr. Chairman.

What I would like to do if I might is just to clear up a couple of things for the record as to why we are here and why this legislation was introduced. Reference has been made over and over again this morning to a "subsidy" and to prices being "driven to cost" as if somehow those are the dominant ideas that frame this debate. For purposes of history, let me point out that this is an effective change in the frame of reference in this debate, and it is a change that forgets where we were before. Where we have been before is in H.R. 6121, 3 years ago, H.R. 5158 a year ago, there was agreement, and let me point out that AT&T supported the agreement in 6121, GTE supported the agreement in 6121 and in 5158, U.S. Telephone was not around for 6121 but supported it in 5158. Mr. McGowan has been consistent in opposing it.

That was the agreement that there were joint and common costs that had to be allocated between long-distance and local service. You supported that, Mr. Brown, you supported that, Mr. Brophy, and today there are about $32 billion worth of overall costs, of which about $8 billion is allocated, joint and common costs is allocated to long distance. There has never been any debate about the fact from all of you, except for Mr. McGowan, there had never been any debate until last August when the FCC comes up and abandons totally the notion of joint and common costs and the allocation of those joint and common costs between local and long distance.

You all may have been reluctant supporters of the notion of joint and common support, but you did support it. The FCC comes in and says, last August: We are going to abandon entirely the idea of joint and common costs and load the total cost onto the local consumer, at which you all jump onto that bandwagon like crazy.

Now, that is where we are in this debate, and the sharing of those joint and common costs between local and long distance has been consistently a position taken by all of you except Mr. McGowan, and now you have abandoned that, and have jumped on the FCC position.

I just think it is important for us to recognize that shift in position, with the exception of MCI. I want to know if you all had any reaction to that. That is, the item that troubles me very much is that there is the shift in gears, because I think there is a significant advantage to you all in doing that.

Does anybody have any reaction to that? Mr. Brophy.

Mr. Brophy. Yes, if I can respond. I think there are two types of costs. There are those that are shared on a usage basis that I mentioned before, and those still would be shared on a usage basis, and then there are the nontraffic-sensitive costs that have in the past been shared on a usage basis also.

I think the concern that has arisen is when you have the cost sharing of the nontraffic sensitive costs by part of the long-distance network, the result is to encourage bypass. If we encourage bypass, then we see higher exchange costs and ultimately higher rates in the future.

Representative Wirth. We had that debate before, Mr. Brophy, if you will remember, when we went through that and others ad infinitum, the bypass issue and where the balance is in the sharing issue. The point was that at that point you all and AT&T and U.S. Tel supported the notion of sharing. You have now abandoned the notion of sharing, following what the FCC started to do in August.

At least that is my understanding of the history of this, and I don't understand why it is that you all had agreed that there would be a sharing of those fixed costs before, the line going from one's house to the central switch, and the wire and the poles, and so on, that those would be fixed costs and there would be a sharing of those costs.

You have decided not to share those costs anymore. I just want to understand how you decided not to do that. Mr. McGowan I understand because he has consistently said he didn't believe that that was a position to be taken. That has been MCI's position, as I remember it, Mr. McGowan, for a number of years.

Mr. **McGowan**. When Mr. Brophy and Mr. Brown started to agree with me, it worried the hell out of me, I'll tell you that.

Representative **Wirth**. Do you agree, Mr. McGowan, that they had argued earlier for sharing?

Mr. **McGowan**. Yes, I do.

Representative **Wirth**. And now you are not arguing for sharing; is that right?

Mr. **McGowan**. That is right. The point they were making is that if you had competition, you would not be able to make any contribution in excess of cost, and thus you would drive up local rates that was a consistent position over the years. It did not prevail. In front of the FCC, and ultimately in front of the courts, that position did not prevail.

No one is denying that we should pay the cost of local switching and trunking and those kinds of things.

The only question was how to allocate the cost of the copper wire that a allows a subscriber to get dial tone—but not necessarily use it.

Representative **Wirth**. My time has expired. Mr. Brown has not had a chance to respond at all.

Chairman **Dingell**. The Chair will permit Mr. Brown to respond.

Mr. **Brown**. Mr. Wirth, I really can't follow this very clearly. There are so many things in those other bills that I am not sure whether the endorsement you put on it of joint and common cost sharing, how that meshed with other things in the bill. I find it difficult——

Representative **Wirth**. Let me just point out for the record, Mr. Brown, that the notion of sharing and that whole access question in H.R. 6121 was worked out very carefully with your people at AT&T, and that is what ended up in H.R. 6121, was supported by them, and that very concept supported and developed with them was translated then into H.R. 5158, so there is a constant theme of that and the support of that from AT&T.

I just want to figure out where the shift in position is if that is not the case. We might leave the record open for any response you might like to make on that front. Consistency is not necessarily the mother's milk of common carrier policy, I understand, but we do the best we can.

Mr. **Brown**. I submit you haven't been exactly consistent yourself with respect to this, and we will be glad to submit our feelings on this subject.

[The following information was subsequently received for the record:]

We have not shifted our position.

In 1979-1980, AT&T and other industry members worked with the House Telecommunications Subcommittee to develop proposals for a workable transition from the separations and settlements process—which the Subcommittee was eager to do away with—to a new system of access charges and a three-part "National Telecommunications Pool", as it was then called.

In bried, H.R. 6121 provided: interexchange carriers were to pay costs "entirely allocable to long distance or related to the volume of long distance calls"; a Transitional Joint Board was established to allocate non-traffic sensitive costs, that is, that portion of the local telephone company's fixed costs for providing local switched service which are not directly caused by long distance usage; a "National Telecommunications Pool" was established to reimburse certain local carriers for a portion of their local distribution costs and toll connecting link costs and to provide transition payments—which were to be phased out over time—subject to the discretion of the Transitional Joint Board; and long distance carriers payments of subsidies—amounts over and above direct costs and the relative use of local switched facilities—were to be capped as of June 1, 1980, and the actual amount of future payments was not to exceed the amount being transferred on that date.

On the key point, the issue of the local subsidies historically provided solely by long distance carriers through the separations and settlements process, the Committee report on H.R. 6121 (House Committee on Interstate and Foreign Commerce Rept. 96-1252; August 25, 1980 at page 75) concluded:

"The bill does not choose any specific cost allocation system. Rather, the Committee intends that a new, fresh review of the entire issues of allocation of such costs be undertaken. The Committee rejects the Commission's tentative view as expressed in its Notice of April 16, 1980, that access charges can simply be grafted on to the existing Separations and Settlements process. After much debate the Committee specifically decided not to adopt in legislation any specific formula such as "marginal cost," "relative use," or the Ozark formula in use today. The Committee felt that such a complex issue should be left to the expert agency, particularly in the first instance, one with state representation. It did agree, however, that this portion of the access charge should not include any subsidies, any amounts over cost. H.R. 6121 provides that any subsidy must be provided through the National Telecommunications Pool. To the extent such subsidies exist today, but are not related to high local distribution costs (NTP account 1), or high toll connecting link costs (NTP account 2), they must be phased out during an appropriate transition designed to avoid significant or undue rate increases."

In essence, what the Committee Report contemplated is what the FCC, with state involvement through the Joint Board, did in its access charge decision in Docket 78-72. In brief, under the FCC/Joint Board approach: directly interconnecting interexchange carriers bear all of the costs directly associated with use; there is an orderly transition over which most of the subsidies contained in today's separations and settlements process which are not related to the provision of long distance service, will, over time, be reflected directly in local service rates. The customers who cause the costs of connecting them to the local telephone central office to be incurred will pay them directly. However, for lifeline service customers, the FCC has provided for a waiver of these charges; the Joint Board's "high-cost factor" represents a workable surrogate for H.R. 6121's National Telecommunications Pool; and the subsidy portion of the separations and settlements process (non-traffic sensitive costs) is capped and phased down over an orderly transition period.

We believe that the current FCC/Joint Board does what the Committee contemplated in 1980 in its report. Moreover, that approach takes into consideration rapidly growing long distance competition and local exchange bypass, which has developed dramatically since 1980. Nothing in H.R. 6121, as we read the bill and the Committee's report, would have precluded the phased-in customer charge approach of the FCC. Indeed, the report explicitly provided that the subsidy portion of the National Telecommunication Pool would disappear as the transition to a cost system is completed. (Committee report, page 78).

As to H.R. 5158, AT&T did not support the bill because it contained provisions which differed significantly from H.R. 6121 in a great number of important areas and did not take into account changes in the competitive marketplace, in the industy and in Bell System structure since 1980 when H.R. 6121 was before the Committee.

Chairman DINGELL. The time of the gentleman has expired. The Chair now recognizes the gentlewoman from Illinois, Mrs. Collins.

Representative COLLINS. Thank you very much, Mr. Chairman.

Mr. McGowan, on the first page of your statement you mentioned that both of the measures, S. 1660 and H.R. 3621, would encourage inefficiency on the part of local telephone companies. Does it seem to you that, under the universal service fund, that a system of paying money to companies for high costs has the potential for actually continually rewarding inefficiencies that you are talking about?

Mr. McGOWAN. There are two ways I believe it would encourage inefficiency, and I say in some cases, continued inefficiencies: One, if you paid money to the telephone company, per se, so that they received the funds and supposedly took care of all users, you have no way of knowing that the funds you are giving them are going to the recipients you want. These bills just hand big gobs of money to the local telephone company.

Second, if you absolutely preclude bypass, you are taking away an incentive from the local phone company to develop the technologies and the efficiencies so it can be competitive. There is no reason why a phone company should not have the capability of providing the most economical local service, and I think by precluding bypass and by giving them general funds, you are encouraging inefficiency.

Representative **Collins**. Mr. Brown, can you tell me how the elderly and the poor in major cities such as Chicago are going to benefit from any universal service fund?

Mr. **Brown**. It seems to me the objective of all of us, Mrs. Collins, is to make sure that the elderly and the poor are not damaged by any shift which is occurring. Undoubtedly under the banner of competition the shift is occurring. It seems to me our joint objective ought to be to make sure that the elderly and the poor are not badly affected by this, and it does seem to me that the lifeline rate principle and the waiver of the access charge on residence customers who cannot afford it does protect the people we are both concerned about.

Representative **Collins**. Might not it be better to earmark the funds for specific types of customers? For example, for the elderly or the poor, people who have very little usage of long-distance lines? Is there not some type of formula that could be developed for that purpose?

Mr. **Brown**. It does seem to me that, as we have talked before generally under the terminology of targeting, it can be done. It can be done by geography, and I think targeting is much more appropriate than a broad-brush subsidy for people who don't particularly need it.

Representative **Collins**. Does the gentleman from MIC agree with that?

Mr. **McGowan**. I certainly do.

Representative **Collins**. Do all of you agree with that?

Mr. **Brown**. I certainly do.

Mr. **Brophy**. Yes, I think it should be a means-tested program.

Representative **Collins**. What rate advantages will we have? I believe all of you have generally agreed that we need not do anything, now, but that we ought to wait until 1983, 1984, 1985. I think you might have even said 1986, Mr. McGowan.

Mr. **McGowan**. I did not say that.

Representative **Collins**. Someone did.

Mr. **Flanagan**. I said that. One advantage is that we would have had time to review the 90,000 pages of tariff filings which have not yet been submitted, and which are due to come sometime between—well, due to come in October. We have no idea what is in that package.

We have no idea what it will do to our rates, to our services, what amount of money we have to charge to others. It is quite unreasonable to expect either the companies or the FCC to evaluate that package in a 90-day period between October 3 and January 1.

Mr. **Brown**. Mrs. Collins, I second that and, in addition I would say if what we want to do is guarantee the revenues, prevent the uncertainty that now exists and is fueling the flames of rate increases, that certainly delaying would be very beneficial in that context. Certainly a delay should be implemented to the extent that equal access is not afforded to the competing long-distance companies, at any rate.

If there are 90,000 pages—and I don't know whether there are or not—the bulk of them are undoubtedly the kind of boilerplate that goes along with tariffs and aren't changed at all, and it will be very easy to find out what the changes are in very short order.

Mr. **McGowan**. One worry I have about a delay is that it implies something extremely significant is going to happen on January 1, 1984. It is actually going to be one of the greatest nonevents, I think, certainly in our industry. I believe people are going to wake up in the morning and are going to live the same life. They are going to pick up the phone and make calls. They are going to make the same local and long-distance calls. It is not going to be significant.

The State PUC's that are trying to dump on you people, as I am sure you appreciate, to offload their responsibilities onto you, will in the meantime not have granted all the rate increases sought by the local phone companies in those States. I am fearful that, if we delay, it we will imply and tell people, "Oh, my God, this is a very important event." It is not going to be a very important event. If there are, however, certain groups, then we should absolutely overcompensate so they are not concerned about it. But I think the rest of us are going to observe that January 1 will come and go, and we are all going to live the same life we have always done before, and so will this industry.

Mr. **Flanagan**. I don't agree with that.

Mr. **McGowan**. I read faster than you can, apparently.

Representative **Collins**. My final statement is that I am very concerned. Very rarely in certain parts of my district do I receive an onslaught of telephone calls from constituents interested in letting me know that they are concerned about this particular legislation and the whole issue of universal phone service.

However, because of the tremendous amount of visual and print media coverage this has received one piece of information seems to have struck a nerve—that telephone rates stand to skyrocket 100 to 200 percent. For the poor and elderly in my district this will be particularly devastating, especially on top of the giant increases in their utility bills, particularly gas bills.

Most of the people in my district come from the South, West Side of Chicago. And what they are able to do on occasion is get on the telephone and say hello to their folks back home. They are really fearful that this is not going to be the case any longer, that their phone bills will get so high for them.

And so I hope that whatever solution we can agree to will be one that is not going to harm the poor and certainly will not cause great hardship on the elderly.

Chairman **Dingell**. The time of the gentlewoman has expired. The Chair recognizes the gentleman from Texas, Mr. Bryant, for 5 minutes.

Representative BRYANT. Thank you, Mr. Chairman.

Mr. Robinson, you are executive vice president of U.S. Telephone, which is exclusively a long-distance provider, as is MCI, and I guess AT&T now; is that correct?

Mr. ROBINSON. That is correct.

Representative BRYANT. In order to provide that long-distance service, you have to have access to the local operating telephone company; is that correct?

Mr. ROBINSON. That is absolutely correct.

Representative BRYANT. You testified, I believe, that AT&T at the present time pays more for that access and that they should continue at least for a period of time to pay more, and I wonder if you would explain why they should pay more.

Mr. ROBINSON. Mr. Bryant, the reason they should pay more is because they get substantially more. One of the aspects that we have talked about throughout this morning and in other forums is that you should pay for what you get consistent with good public and social policy. In order to use the system, as I have stated here earlier this morning, in order to access for AT&T, you have to use only 10 or 11 digits.

To access the system that we use, you need to use 23 to 24 digits, which is a substantial inconvenience to our customers, and because of that inconvenience they are willing to pay us substantially less in terms of rate.

The quality of the interconnection is a substantially lesser grade. Hums and hisses essentially result as a function of that lesser grade of interconnection, and as a function of that our customers are willing to pay us under substantially lesser rates.

Representative BRYANT. Wouldn't it put them at a competitive disadvantage to continue to pay higher rates?

Mr. ROBINSON. Absolutely not. There is a substantial competitive advantage today, in terms of convenience, in terms of the quality of the transmission, in terms of the markets that they can access. They are at a substantial competitive advantage, and when we get truly equal access we would be delighted to participate in that advantage.

Representative BRYANT. The modified final judgment requires equal access by 1986, but your testimony seems to reflect some doubt in your mind as to whether or not that is going to really ever happen. Would you elaborate on that?

Mr. ROBINSON. Well, we are optimistic that it can be done, but as has been stated here earlier this morning, there is lots of work to be done in order to accomplish that. Two things I would like to say on that. To the extent that equal access is provided we will avail ourselves of it, and to the extent it is provided, we would be delighted to pay the same rates to provide equal service.

To the extent that it is delayed, we don't wish to pay for something that we are not getting, and to the extent that it ultimately is not equal access, and it is our understanding that in many locations equal access will not be available no matter what, but to the extent that it is not equal access we don't wish to pay for it.

Representative BRYANT. Do you know or would you comment on what the effects on the local rates would be if your proposal to continue making those who have better access pay more was adopted by Congress?

Mr. ROBINSON. Quite frankly, in terms of the effect on the rates, I couldn't quantify it for you, but what we are really talking about here, and really to address a comment that Mr. Wirth made earlier, we haven't changed our position on joint shared cost at all. We remain completely consistent.

Whatever that cost is for the long-distance telecomunications carriers must pay has to be allocated fairly between those. And so if there is one long-distance telecommunications carrier which has a substantial advantage, he ought to pay for it. Whatever that percentage of the cost bill is should be allocated to them on some rational basis related to value.

Representative BRYANT. Would the proposal ease pressure? Could you make a general statement that it would ease pressure on local rate increases?

Mr. ROBINSON. In one sense I agree with Mr. Bill McGowan on that issue. Come January 1, in that sense at least it will be a non-event. The underlying economics haven't changed, and so if we implement the proposal to delay the implementation of the new access charge plan, and if we implement the proposal to continue with MPS as the methodology by which revenues flow to the local access aspect of the business, that will reduce the uncertainty and it will have a very positive effect in controlling the local rates.

Representative BRYANT. Mr. McGowan, would you like to comment on any of the questions that I asked?

Mr. MCGOWAN. I concur with Mr. Robinson. I would like to make an additional point. AT&T has been the one that has caused the local telephone company to structure itself in such a manner as to provide both local and long distance. For example, AT&T was in control of the numbering plan requiring 10 digits.

AT&T receives its interconnections from a local phone company in a four-wire trunk side arrangement, whereas we are interconnected on a two-wire station side. We literally—so you understand—we literally get the telephone service that you get at home. We get two wires and a phone number.

Now, we may get 50,000 of them scattered around the country, or more, but we get the same service that you get in your office right here on the Hill. We are asked to pay $280 going up to $450 per line per month for that service? That is unreasonable.

Mr. ROBINSON. I second that, Mr. Bryant.

Representative BRYANT. Mr. Brown, do you want to respond?

Mr. ROBINSON. In the first place, better connections are now offered by the telephone companies to these people, but they don't choose to take them. It would be much easier to complain about the problem than to take the better connections.

Representative BRYANT. Is that correct?

Mr. ROBINSON. U.S., telephone talking about AT&T, has been a substantial issue and we take the intersections wherever we can get them.

Mr. MCGOWAN. One is too expensive, the other one is completely not available.

Chairman DINGELL. The time of the gentleman has expired. The Chair now recognizes the gentleman from Ohio, Mr. Oxley.

Representative **Oxley**. Thank you, Mr. Chairman.

Mr. Brophy, the Packwood-Dingell bill would still continue the subsidy much like we have today, and it seems to me that that would encourage bypass. I know you commented earlier about the potential problems with a penalty that would be assessed for those companies that would seek to bypass the system, and I think that you made some reference to perhaps some kind of constitutional problem as well as a practical problem.

Yesterday we had testimony from the Governor of Indiana, and the Governor indicated that he supported what he called a penalty for bypass. I wonder if you could address that particular problem as it relates to the Packwood and Dingell bills, and tells us how we might deal with the perceived problem of encouraging bypass by subsidizing local service by the long-distance rates.

Mr. **Brophy**. It is a terribly difficult problem. I did attach to my testimony a copy of an opinion from the law firm of Sullivan & Cromwell raising a series of problems, questions, including constitutional questions.

Representative **Oxley**. I can't hear. Will you speak a little louder?

Mr. **Brophy**. I say I did attach to my testimony an opinion of the law firm of Sullivan & Cromwell that raised a number of problems and questions, including constitutional questions. We have been trying to find solutions to those problems and questions, and to date we have not been able to.

My great concern would be that we not put in place here a system that is going to be challenged by all those people who would be subject to the tax or charge, so that we find ourselves at some time in the future having some $10.7 billion or some portion of that in doubt. The telephone companies, which are very large users of capital, find uncertainty to be the most difficult thing to live with.

Representative **Oxley**. I thank you.

The general concept, though, of subsidizing local rates is in and of itself an incentive for bypass, is it not?

Mr. **Brophy**. Yes. If the interexchange rates are forced up in a way that is related to usage, and encourages those large users to bypass the local system, then that drains revenue from the local system without draining equal amounts of cost, and the result then is to increase the cost of local service and the rates to those people who remain on the local system.

Representative **Oxley**. How do we define bypass? If I have a two-way radio and I use that, is that bypass, or if I use the U.S. mail instead of picking up the telephone, is that bypass? And is it good public policy to penalize a company, for example, that finds it much more economically beneficial to itself and its shareholders to indeed bypass, than to participate in the existing system?

Mr. **Brophy**. We believe that the decision probably in the last analysis can only be made on an economic basis. There is that problem of definition that you mentioned, whether somebody who uses a CB radio at a State line is bypassing or not. I just don't know. You do have that very difficult problem of definition, in an industry where technology is changing so quickly, that something may well come along today, or tomorrow, and you would again have to define bypass so that the new technology is either inside or outside the limits of bypass.

Representative **Oxley**. Mr. Brown, would you care to comment on that?

Mr. **Brown**. I think I agree with what Mr. Brophy said here. It is very, very difficult to define, more and more difficult to administer, and we haven't been able to figure out a way which would give us confidence that bypassers would be swept into this net.

Representative **Oxley**. Do any other of you gentlemen wish to comment on that particular issue?

Mr. **McGowan**. The technology Mr. Brophy mentioned is here. You have ways today to send a 30-word message to a pocket pager. It is digitally stored and can be read. That is exactly the same as if you call somebody on the phone with a one-way message. The way technology is evolving, I don't think you could eliminate bypass—it certainly wouldn't make any commonsense, and it certainly wouldn't be good policy, but I doubt whether technologically or practically you could even try it.

Mr. **Flanagan**. It doesn't have to be technological. It is equally bypass if you use a courier service to get that same message to its destination as if you use Bill's pager item. I don't know how you can draw a line to say these are those who will pay a tax. But there are those other people here who will not.

Representative **Oxley**. Thank you, Mr. Chairman.

Chairman **Dingell**. The time of the gentleman has expired. The Chair now recognizes the gentleman from New Jersey, Mr. Rinaldo.

Representative **Rinaldo**. Thank you very much, Mr. Chairman.

Mr. Chairman, there are a number of things going on which make it unclear to me, and I guess to everyone else, how much telephone service is going to cost in the future. First of all, as I look at the problem, we have no data showing the impact of FCC decisions on the ability of low-income people to continue their telephone service. In fact, as you know, the FCC has just revised its original access charge decision, in order to mitigate somewhat its impact on local telephone rates.

Second, long-distances rates, we just heard, are expected to come down beginning next January.

Third, the telephone companies are beginning to provide low-cost lifeline service to those customers who do not use the telephone heavily.

Fourth, it is now possible, as we know, for telephone customers to purchase rather than lease their phones, and the telephone bills of those who purchase their phones will decrease by the $2 to $3 per month lease payment that has been included in their phone bills in the past.

Despite all of this, some telephone companies have recently asked their State regulatory commissions for approval to increase the average local telephone rates in their States by 100 percent or more. In a few cases, as a matter of fact, rate increases of 150 percent to 200 percent have been sought, and I guess this has caused the flurry of bills that have been introduced to end up in the hopper.

I would like to ask Mr. Brown, are you familiar with these rate increase requests?

Mr. **Brown**. Yes, sir.

Representative **Rinaldo**. Let me ask you another question. Have any increases throughout the country, to the best of your knowledge, 100 percent, 200 percent or any rather high increases, been approved anywhere?

Mr. **Brown**. No, sir, I have not seen any such increases approved. The average approval for this year has been in the order of 37 percent of the request, of what the companies feel they need. Now, I don't mean to indicate that these companies are asking for more——

Representative **Rinaldo**. Will you get a little closer to the microphone, please?

Mr. **Brown**. I don't mean to indicate that these companies are asking for more than they need, because they do feel that their rate of return authorization is low. They have not in many cases been able to earn that rate of return, by virtue of regulatory schemes, and I am not denigrating the decisions of the telephone companies for what they will need in 1984 and 1985, and so forth, when they are on their own. The facts are, as I understand the regulatory people at the witness table yesterday indicated they rarely grant what the companies ask, and I guess it is true for power companies and gas companies and other regulated organizations.

Representative **Rinaldo**. As I understand it, the telephone companies who are seeking these, what I would term massive, exorbitant rate increases are blaming the FCC's access charge and depreciation decisions as well as the AT&T divestitute. Now we know that the FCC decisions do not require rate increases of 100 percent or 200 percent, but is there anything in hearing in divestiture that requires local rate increases, or is this just a scarecrow that is being thrown out there?

Mr. **Brown**. It is hard for me to talk in general terms and not be wrong in all the individual jurisdictions in this kind of a situation. Jurisdictions differ very, very sharply. If you go over the history of rate increases or lack of rate increases, in some jurisdictions you will find that the commissions have in some cases authorized nothing, and rate increases, rate cases have gone on for 12, 14, 16, 18 months to end up with a zero decision on the part of the commission.

When that happens in a certain year, in the following year the companies must go back in for larger increases because of that kind of regulatory treatment.

On the other hand, there are regulatory agencies who do not operate on that sort of basis, and carefully consider what companies need, and give them rate increases which correspond to inflation pressures, depreciation pressures, et cetera, and so the situation varies among jurisdictions very sharply.

Representative **Rinaldo**. Are you saying, then, that in effect the massive rate increases that some people predict as a result of the access charge and depreciation decisions as a result of divestitures, as a result of anything, really are not going to come about, and that in your view only a very small percentage type of increases will be approved by State regulators?

Mr. **Brown**. Let me put it this way, Mr. Rinaldo. Certainly the history would indicate that these kinds of rate increases are not going to be approved in their entirety by commissions, and in any event, the commissions have full control of the matter.

Representative **Rinaldo**. What do you expect the average increase will be? Do you think it will continue at 37 percent or do you think over the long haul it will drop down and correspond roughly to the equivalent of the annual inflationary rate that has taken place over the past few years?

Mr. **Brown**. Mr. Rinaldo, I am on record in this chamber as saying that over a period of time, were I to be able to average rate increases at a time when this subsidy is being removed, that if the telephone companies received in the order of 8 to 10 percent over 4 or 5 years on an orderly basis, it would manage to shift these cost and price problems in their entirety.

Now, one of the difficulties is, of course, that these rate increases are not generated on that kind of a basis. Nonetheless, I stand by what I said.

Representative **Rinaldo**. Thank you.

Chairman **Dingell**. The time of the gentleman has expired. The Chair recognizes now the gentleman from Tennessee, Mr. Gore.

Representative **Gore**. Thank you very much, Mr. Chairman.

I would like to welcome this distinguished panel. I appreciate your testimony. I am concerned about this issue. It is extremely complicated, but it seems to me there is a very simple injustice that is about to occur if the current plan is implemented. You all have indorsed it for obvious reasons.

What we are about to establish, unless the Congress acts, is a telephone system that is partly competitive and partly exploitative. You are asking, and the FCC is asking, local telephone customers to pay 100 percent of the cost of maintaining equipment that you use to deliver your service. That is not fair. I speak, of course, of the local loops and the joint facilities that are used both by local calls and by long-distance calls.

Now, the principles of joint cost accounting seem complicated, but really aren't that complicated. Joint cost accounting is more an art than a science, and people have heated arguments about how to allocate joint cost as between common users, but I know of no one, no one, who argues that it is justifiable to take joint and common costs and allocate them 100 percent to one party and zero percent to the other. You are asking for a free ride on the backs of local telephone users.

You pay for the connection from one city to another, but you can't deliver your service until you can get into the home or into the business. In order to do that, you have to use the telephone lines and the telephone poles and the equipment of the local telephone exchange. In the past always the cost of that joint facility has been shared by the long-distance provider and by the local user. What you are asking is for a free ride. You want to escape all of that cost and put all of it on the backs of the local customers. How in the world can that be justified? Mr. Brown.

Mr. **Brown**. Mr. Gore, I think that what has happened here in the competitive environment in the long-distance business is being completely ignored in that kind of a statement. As long as there is an uneconomic cost, price being applied to long-distance charges, there can be no subsidy to anything else. As long as there are abilities for people to bypass, there can be no subsidy from one service to another or the economics of the matter would drive the telephone system itself into great difficulties.

Representative GORE. But that doesn't answer the question, Mr. Brown.

I don't understand how you can justify. Let's take the case of a senior citizen in Tennessee who has a local telephone, doesn't make a lot of long-distance calls, calls her neighbors, use the local telephone loop. Why should that senior citizen pay 100 percent of the cost along with other local users of equipment that you are using to make a great deal of money on?

Mr. BROWN. The problem is that that wire has to be there for local service to begin with, and the costs are not being covered by that customer now.

Representative GORE. Well, it has to be there for long-distance calls to be made.

If you and I buy a car, you and I buy a car, Mr. Brown, we are both going to use it, OK? And we agree to share the cost.

A couple of years pass and you come to me, or I come to you, and I say, "Look, it turns out you are using this car more than I am. You are using it 75 percent of the time and I am using it only 25 percent of the time. I have got an idea. Why don't you pay for the whole car because it is going to be there anyway, and in that way I will get to use it for free."

Would that strike you as fair?

Mr. BROWN. No, that is not fair and it is not even germane.

Representative GORE. That is what you are doing. That is what you are doing to the local telephone customers. That is exactly what you are doing to the local telephone customers.

Years ago you said to the local exchanges, "Look, let's build a telephone system. We will use it and you will use it. We will use it for long distance and you will use it for local and we will share the costs. We are both using it."

Now, years have passed by and you say, "Look, you are using it more than we are. I have got an idea. Why don't you pay for all the cost and we will pay for nothing. It has got to be there anyway for you to use it, and we have got these other things that we are interested in."

Does that strike you as fair, Mr. Brown?

Mr. BROWN. Don't say "I have got an idea." I say it is not my idea.

Representative GORE. But you have endorsed it, you are supporting it, and all of you are pushing it, and it is not fair.

You are absolutely right. And I don't want to slander you by saying it was your idea, because it wasn't, because in the past you have always accepted, everybody here with the exception of Mr. McGowan, I think, has in the past always accepted the notion of shared costs, because it is basic fairness.

What I have got a problem with is now you see an opportunity with the restructuring of the telephone industry, "Ah, now we can completely redo the rate base, we can completely redo the structure of the industry, and this is a great opportunity to dump 100 percent of the shared joint common costs of the local plant facility on the local consumers, and we will get off scott free."

It is unfair, and that is the simple injustice which is going to cause the House and the Senate, in my opinion, if I read the political currents correctly, it is going to cause the passage of legislation to prevent this unfairness.

Mr. McGOWAN. Mr. Chairman, may I comment on that?

Chairman DINGELL. The time of the gentleman has expired.

I think Mr. Brown ought to be able to respond.

Mr. BROWN. I have no further response.

Mr. McGOWAN. May I comment?

Chairman DINGELL. Mr. McGowan, of course.

Mr. McGOWAN. I believe you are mischaracterizing the cost structure in our industry.

There are two concepts involved. One is the cost of getting to the network, the line that goes from your home or business to the closest telephone central office. That is like an electrical hookup charge, like a sewer charge, that is like any other utility connection charge. You pay in every other instance, you pay to access service.

There are, in addition to that, usage costs—switching costs, trunking costs—within the local network. No one is proposing that people who occasion those costs shouldn't pay them. We are going to pay them; Lord knows we pay enough today for them.

What the FCC is talking about is that connection charge, just the connection. You pay for it in every other utility, everbody always has. If I want gas, I pay a connect charge. In addition, I pay for the gas I use.

If I want electricity, if I want sewer, if I want utilities in the United States—a common fact, I pay to connect to the system. You pay electrical charges. I just got through paying a big electrical charge to get into the grid. So the connection charge is what we are talking about here, not the usage, not the charges for switching and trucking. We are going to pay for that. We always have.

You are now saying that, unlike every other utility in the United States, you want to have someone pay part of the local guy's costs. Well, he is going to end up paying it eventually anyway.

The users pay for everything. I don't care whether it is gas, electricity or power. Obviously, users end up paying for it directly or indirectly. They pay for it up front. They pay for usage. And what you are characterizing is just simply not true.

Representative GORE. Mr. Chairman, with the indulgence of my colleagues, if I may very briefly respond, that is just not the case. Some users will pay and some users will not. You all are big in having the economics of the marketplace drive the decisionmaking process, but you are asking all users of local telephone service to pay all of the costs of the local facility whether or not and regardless of the extent to which they use long-distance services. The facts remain that those switches and the facilities that get you from one city to the other are shared in cost but the local facilities are not.

Thank you, Mr. Chairman.

Chairman DINGELL. The time of the gentleman has expired.

The Chair now recognizes my friend and colleague from Michigan, Senator Riegle.

Senator **Riegle**. Thank you, Mr. Chairman.

I have really two things I would like to inquire about. One is a very simple question that is not easy to answer, and that is, what should local unlimited phone service cost? What should that cost, looking out over the next year or two? What is a fair figure?

Mr. **Brown**. As you point out, it is not a very easy question to answer.

I think it depends primarily on what that service costs in the geographical area involved, and those costs vary widely. So it is impossible for me to answer that question except on a broad basis.

Senator **Riegle**. Let me try to get you to think about it a different way.

I understand the way you feel compelled to approach it, but approach it from the consumer's point of view.

I mean, should basic service for a person to connect and make phone calls cost $10 a month, $12 a month, something in that range? Is that a fair figure?

Mr. **Brown**. For today's service, let me put it this way. In Michigan the average telephone bill is $34.76 for a resident.

Senator **Riegle**. Of course, a lot of that is long distance.

Mr. **Brown**. I was going to say that. Some $13.90 is long distance itself, and there are other different kinds of charges in the remainder. This thing varies broadly between states.

In Iowa, the total bill is some $30, and in Arizona the bill is $36. So it is hard for me——

Senator **Riegle**. Let's get down to the basic service without the add-ons. I am just talking about the costs for somebody to plug in and get basic local service.

Can we establish some kind of a fair figure or even a narrow range that we ought to shoot for? Because that is one way to deal with this problem.

Mr. **Brown**. Sorry, I don't have any way of suggesting what a charge should be, because the costs vary so broadly between geographic areas.

Senator **Riegle**. It seems to me that maybe what we ought to be trying to do here is to find some way to deal with that issue. I mean, we do it in a sense with these lifeline systems, which exist in my State, and some of the other States.

Mr. **Brown**. I think one of the things that is involved here is the involvement of the local commissions in setting local rates, and I think that is where it ought to reside. That responsibility ought to reside there.

I really don't think Congress can effectively set local rates.

Senator **Riegle**. That is what I guess we are going to decide here.

The question was posed earlier as to whether or not January 1, 1984, is going to be a nonevent.

We didn't hear from everybody on the panel, and I am told that there was some disagreement on that.

Who there among you think that that date is going to be a very significant date, and that events are going to change quite fundamentally at that point?

Mr. **Brown**. If I understand what Mr. McGowan meant in the case of a nonevent, I understand him to mean that the shift in charges, which would be involved if the FCC orders go in as now scheduled, if the divestiture goes on as now scheduled, the shift in charges is not going to be so significant as to be a major event for the customer. I believe that is what he referred to.

Mr. **McGowan**. That is what I did refer to.

Senator **Riegle**. Does anybody have a different view?

Mr. **Flanagan**. Yes; Robert Flanagan. I have a different view.

I think there are a number of analysts who follow this industry who believe there is going to be a very substantial shift in charges that will affect certain segments of the industry in any event. I can well imagine they would affect my company.

I think rather than speculating about this, because we may be right or we may be wrong, we ought to wait until we have the information and see what it tells us.

I refer again to the 90,000 pages of tariff filings which we are all waiting to receive from AT&T. We are going to learn something from that, and it will add to the other things we are learning from the filings that are going on before the States.

I think when we have those facts, we can try to deal with them, instead of trying to guess in advance about something which we will after a while know factually.

Mr. **Brown**. I think we are talking here about the residence customer, at least Mr. McGowan, I think, was referring to the residence customer, and so was I.

Senator **Riegle**. My time is up, but does anybody else have a view on that subject that they want to express?

I gather not, Mr. Chairman.

Chairman **Dingell**. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Pennsylvania, Mr. Ritter, for 5 minutes.

Representative **Ritter**. Thank you, Mr. Chairman.

I would like to ask the panel in what ways they feel those users who would be bypassing, who would be taxed under the Wirth approach, in order to reduce the incentive to bypass, in what ways could those users avoid being found? And indeed, how we are going to be able to find all these users, and then enforce the tax on these users?

Are mail substitutes and two-way radio bypassers going to be encompassed in a bypass tax? How complex is this, and what are some of the problems that might be involved in attempting to tax bypassers?

Mr. **Brown**. If I may start on this, I think the net, trying to scoop in all the bypassers, is going to have a great deal of trouble.

Let me speak technically for a moment. A satellite can handle literally hundreds of thousands of calls, calls which might well have been diverted from the local telephone network by virtue of dishes on buildings, antenna dishes.

A reasonable question is, Should the taxing or should the bypass charge be based on the number of calls they have that particular day, or the capacity of the satellite, or whether or not there is data being transmitted over the network which involves a great deal of information, and the technical problem of trying to understand how to do this has not been solved by any of us.

Representative **Ritter**. Where would the personnel and the resources come to do what seems to be a massive monitoring effort to somehow keep up with the bypassers, so that you can enforce and collect and administer a taxation program?

Mr. **Brown**. I don't know where such resources would come from, and how they could carry it out in an equitable manner. I think it would soon become a real jungle.

Mr. **McGowan**. Part of it is that when we bypass, for example, we don't even know it sometimes. Let's say I go into our system and look for messages internally, I don't know where that message is. It may be stored right here in Washington on a small computer. That is a local call, that is not bypass; but it might be on a computer in Chicago. So when you search for it and my software looks at it and finds it in Chicago, it gives it to me.

In one case you should pay some kind of a fee. In the other case, it is local. I don't know; no one knows.

Maybe the system could change the software program where all of a sudden it would report your having a bypass somehow. But that is crazy. I mean, it just can't work.

You say, let's do it for voice and not for data. Well, believe me, we transmit on a fiber optics system and there are 400 megawatts over that system, I can't tell what is voice, what is data, what is video and I don't want to know. The system doesn't want to know. It is all going digital.

Representative **Ritter**. Could this have the impact of squashing high tech development in new bypass areas?

Mr. **McGowan**. The best way to answer that is to say if this had been in place for the last 10 years, the answer is decidedly, obviously, it would be yes. Nobody would build the stuff.

Why would somebody develop digital termination service? Why would somebody develop——

Representative **Ritter**. You are talking too fast.

Mr. **McGowan**. Why would someone develop existing technology we have knowing that he could never use it or he would pay a penalty if he did. If this had been in effect for the past 10 years, the answer is we would not have most of the technological——

Representative **Ritter**. So the bottom line here is that this kind of legislation could end up squashing high tech development and the jobs that go with it, could end up costing consumers more, the very thing that the authors of this approach are trying to avoid with their honorable intentions?

Mr. **Flanagan**. It could even squash job opportunities for this country, which would follow from the squashing of those high technologies.

The best we could hope for would be that it won't work. If it does work, it will squash these high technologies which we need, which other countries are certainly going to go forward with, and those export jobs would simply go elsewhere.

The best we could hope for is it won't work or that it will be applied quite unfairly to some particular forms of bypass which happen to have been identified by this legislation, and then the next form of bypass that comes around will not be taxed.

Representative **Ritter**. It would seem to me too that the phone rates that the country pays are inevitably paid by the consumer. There is no secret pool of money out there that doesn't belong in somebody's wallet to start with, and it would seem to me that if you tax one side, the other side is going to pay. If you tax long distance or bypass, those consumers using that will end up paying.

Was that my time, Mr. Chairman?

Chairman **Dingell**. That is the gentleman's time, but the Chair will let the gentleman finish his question and let the gentleman respond.

Representative **Ritter**. Thank you. I just have one quick question.

Mr. Brophy mentioned something about a constitutional problem, which I think it was mentioned in passing, and I think those of us up here are probably interested as to what he had in mind.

Mr. **Brophy**. I attached to my written testimony an opinion from the law firm of Sullivan and Cromwell that raised the question as to whether or not the tax could be treated as a fee or user charge, and concluded that it probably couldn't and used for the purpose for which it was designed. And it then raised the question as to whether or not, if it were a tax, and if the tax base—the persons on whom the tax falls—were not clearly defined, and if the tax rate was not clearly defined, but rather those decisions were to be made by some other body, that would be an unconstitutional delegation by the Congress of the taxing power.

Those are the difficult questions that are raised.

Representatie **Ritter**. We could always form some new committees here to dream up the rates and staff them with additional personnel. That is not impossible. We seem to have done things like that before.

Mr. **Brophy**. It may be possible to draft language. My big concern has been that whatever the end result be, that it not be one that encourages those people who would be subject to the tax to challenge it in the courts, and the telephone industry would be found with years——

Representative **Ritter**. But that would provide more jobs for lawyers, which is the largest growth industry in this town. Forget high tech.

Thank you, Mr. Chairman.

Chairman **Dingell**. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Minnesota, Mr. Sikorski.

Representative **Sikorski**. No questions, Mr. Chairman.

Chairman **Dingell**. The Chair has a few questions.

Mr. Brown, you had a very interesting comment in your statement and I observed a similar comment in Mr. McGowan's statement, and it goes something like this: "State regulatory commissions continue to have ample authority to assure that the explosive competition that now exists in the telephone communications industry does not jeopardize universal service."

What authorities remain with your State public utility commissions under the FCC plan?

Mr. **Brown**. They retain all local rate authority except——

Chairman **Dingell**. They have lost depreciation responsibilities over the local rates, have they not? Hasn't that been preempted by the FCC?

Mr. **Brown**. Well, sir, I believe they never had that. As long as I have been in the business, the FCC handled——

Chairman **Dingell**. There was a time way back when they had but they don't have it now.

Mr. **Brown**. I think the State PUC and the Federal Commission come together and decide what the depreciation rate ought to be.

Chairman **Dingell**. The board which is rated for FCC dominance.

Mr. **Brown**. Well, sir, I understand they read the 1934 act to have a uniform system of accounts and depreciation is surely a part of that.

Chairman **Dingell**. So that is really decided by the FCC and they have the authority to deal with that issue?

Mr. **Brown**. Yes, I think you are correct. The depreciation and the $2 access charge, it seems to me, are Federal Communication Commission matters. The rest of it is put within the control of the States.

Chairman **Dingell**. Now, they also lose control over access charges, do they not?

Mr. **Brown**. The resident's $2 access charge, yes, sir.

Chairman **Dingell**. So that is fixed by the FCC. The only thing, then, that they can deal with is the traffic sensitive issues and costs. That is all they get to deal with, isn't it?

Mr. **Brown**. The statement I think was made that they have everything else, everything else under their control in the States.

Chairman **Dingell**. What I am trying to find out is, what is everything else? It doesn't sound like very much to me.

Mr. **Brown**. The cost of using the switches.

Chairman **Dingell**. They don't get to deal with the fixed charges that relate to the switch. They get to deal with the costs of repairing the switch, or something of that kind.

Mr. **Brown**. They get to deal with the usage of the whole network, which supplies dial tone, which provides the switching, which makes the connections. They get to deal——

Chairman **Dingell**. That is a relatively piddling item, is it not?

Mr. **Brown**. No, sir, it is not.

Chairman **Dingell**. The big items here are going to be the access charges and the depreciation. What remains is going to be relatively trifling, and will affect the rates only slightly, isn't that right?

Mr. **Brown**. No, sir. The local charge in Michigan now averages about $14.51. That does not include this $2 access charge. It includes all the depreciation, and so on——

Chairman **Dingell**. But the depreciation you told me is going to be fixed by the FCC?

Mr. **Brown**. It has been fixed by the FCC in the past. It is a small part of that anyway.

Chairman **Dingell**. Depreciation, as I understand it, is a rather large item.

They have lost control over depreciation. They have lost control over the access charges. You have told me that the $14 local service charge includes depreciation.

I am trying to figure out what remains in terms of fixing the rate of the household user or any other user.

Mr. **Brown**. I guess I can only repeat everything else.

Chairman **Dingell**. Everything else, but what is everything else?

Mr. **Brown**. If you are asking me what portion of that $11.14 is depreciation, I can't tell you from this table, but a small portion of it is.

Chairman **Dingell**. Depreciation, as I gather, in Texas, and I don't have Michigan's figures, is $450 million out of $1.2 billion. That comes out to be over one-third.

Mr. **Brown**. The depreciation rates are not set every year. They are set every 3 years by a joint discussion between the PUC and the Commission.

The third party in that is the telephone company which asks for certain depreciation rates. I believe the number in Texas was that which the Texas telephone company thought was desirable, thought they needed with respect to the depreciation, not one which was authorized.

Chairman **Dingell**. As I understand it, yesterday, all the public utility commissions testified that they do not have sufficient authority to deal with explosive competition or to protect their ratepayers because the package that has been prepared for them by the FCC leaves them total authority to address the question of rates or the question of competition either intrastate or interstate.

Mr. **Brown**. I realize that is what some of them say, but what I think the facts would reveal is, aside from these two things we mentioned, they have full control over local rates.

Chairman **Dingell**. But I have been asking you to tell me what is everything else is and you define "everything else" as being everything else.

[The following information was subsequently received for the record:]

American Telephone and Telegraph Co.,
New York, N.Y., August 3, 1983.

Hon. John D. Dingell,
Chairman, Energy and Commerce Committee, House of Representatives, Washington, D.C.

Dear Mr. Chairman: During the Joint Hearing last Friday on the various pending universal service bills, you asked three questions to which I want to respond immediately.

Depreciation procedures.—Some people seem to think that the FCC has "preempted" regulation of depreciation for Telephone companies. That's not so. They have had that authority since the Communications Act of 1934, (Section 220(b)). This has recently survived court challenges. Under Section 220(i), no changes in methods or rates are made without the FCC considering the views and recommendations of the State Commissions.

The setting of rates for many years has been on a three year cycle, with one-third of the Bell companies being reviewed each year. Three-way meetings with FCC-State-BOC representatives are held to review requests and make recommendations which the Commission considers in determining the depreciation rates.

Relationship of depreciation expense to PUC regulatory authority.—You asked me about what the State regulators have left to regulate if the FCC has depreciation rate authority. Although I could not recall at the Hearing what portion of local rates is attributable to depreciation, I have found the number to range from 10 to 17 percent. Michigan, at 13.3 percent is at the median.

BOC services remaining under State regulation.—You asked me what State PUC's have left to regulate after the $2 access charge and the FCC prescribed depreciation. I answered "everything else intraLATA." A list of "everything else" is attached, indicating that they control prices for the bulk of Telephone company services.

I hope this information will be helpful.

Sincerely,

Charles L. Brown,
Chairman of the Board.

POST-DIVESTITURE BELL OPERATING COMPANY SERVICES PROVIDED IN THEIR INTRALATA AREAS SUBJECT TO STATE REGULATION

Local exchange: Local measured service (business and residence), premium flat rate.

Usage services: MTS, WATS, 800 Service (inward WATS), Enhanced WATS, 900 services, such as DIAL-It (976), 911, optional calling plans.

Access services: Network access, special access, special features, Billing services, collection and other special services.

Packet switching services.

Central office based services:

Centrex (various levels of service), Touch-Tone, custom calling features (e.g., call waiting, call forwarding), remote call forwarding, dial up teleconferencing.

Operator services; Custom call handing, customer listing information services, special billing, teleconferencing.

Public telephone services: Coin telephone service, semi-public service, charge-a-call.

Directory: White Pages, Yellow Pages (revenues in certain states), sale of directory listings.

Dedicated services: Dedicated channels, dedicated access, off-premise extensions—PBX and other, sub-voice grade services, voice grade services, digital services DATAPHONE digital service, high capacity digital service, wideband analog channels, fire and other alarm channels, closed circuit program services (video and audio, e.g., for wired music), power metering and control channels.

Mobile radio services: Mobile radio service, cellular mobile radio bellboy paging service.

Mr. **Brophy**. Can I address that in part?

First of all, the States will have control over all expense items related to local service. They will also have control over the cost of the intrastate access charge, because there will be an access charge for intrastate service, so that they will be controlling a major portion of the telephone bill.

If I can say a word about depreciation. If the thought is that the States would somehow hold down depreciation expense, I can't imagine anything that in the long run is going to drive up the cost of the local ratepayer more.

That is a very short solution with a very damaging long-term effects because it builds up the rate base and deters the utility from deploying new technology.

Chairman **Dingell**. I am not advocating that. I am trying to find out what control remains. There are also access charges to the intrastate long-distance portion of the system that will essentially mirror or be a shadow of the interstate access charges which will be fixed by the FCC, correct?

Mr. **Brophy**. We hope that will be so, Mr. Chairman, but that is not mandated.

Chairman **Dingell**. Well, I think the hope will become the reality. Gentlemen, the Chair's time has expired.

The Chair will start recognizing my colleagues again in the order of appearance and I hope we will be able to revisit these questions.

The Chair recognizes again my good friend, the early bird of this operation, Senator Packwood.

Chairman **Packwood**. Mr. Brown, the present subsidy is about $11 billion?

Mr. **Brown**. Yes, sir.

Chairman **Packwood**. I take it all of you, and I will include Mr. Brophy in this, I mention him because he is, of all of you, the only one left after divestiture that will be heavily involved in the local phone business.

All of you have no fear about the loss of universal service if the FCC's access charge—and I don't mean the $2 we are here referring to until 2 days ago that was a $2 minimum that was going to go up each year—none of you have any fear about the loss of universal telephone service to the rural and residential areas, even if all of the costs that everyone is talking about are imposed on local users; is that correct?

We can start with Mr. McGowan.

Mr. **McGowan**. I think there is very little fear, with the exception of people who are poor, on welfare, and if the costs go up excessively, I think there is danger there.

I think that Congress shares my concern to do something and target that group. For 99 percent of the people with phone service, of which 92 percent of our population apparently do, I do not have concern.

Mr. **Flanagan**. I think it is a social issue which Congress should address. I would not be in the position of some of the others to be able to say that only a small portion of the country will be affected because I don't believe we know enough about the outcome of the work that is underway at present.

It may be that 99 percent are not going to be affected, maybe a considerably larger group will be affected. Certainly it is a social issue which needs to be addressed.

Mr. **Brown**. The FCC order takes care in large measure of the high-cost areas by the fund which is set aside for that purpose. The order permits waiver of the access charge for residence customers who are judged to need it and it seems to me that is a good way to attack the problem.

Mr. **Brophy**. We share your concern and the last thing we want to see is anybody drop off the network. We do believe that it can be covered through a means tested entitlement program and through the lifeline service.

Chairman **Packwood**. Mr. Robinson.

Mr. **Robinson**. I think the real answer is that we don't have sufficient information yet to know. Obviously, the social issue has to be addressed concerning lifeline. But with respect to other users, I don't think we have sufficient information to know.

Chairman **Packwood**. You all want universal service. All of you are in the long-distance business and it is a social policy. Do you think universal service will continue?

You have expressed very few fears even with what we regard as significant increases that are bound to go into effect, therefore, so long as universal service will exist it is in all of your interests, isn't it, with the exception of, perhaps, Mr. Brophy, to have long-distance charges as low as possible from the profit standpoint of your own costs, so long as you can continue universal service; your interests are best served by as low or no subsidy charge on long distance for local rates?

Mr. McGowan?

Mr. McGowan. Our interests are served by having the efficiencies of my operations, technologies, and economy of providing my services reflected in the rates I charge for those services. For me just to have low prices, I use up my profit.

I don't necessarily need to have prices so low that I am not profitable, but certainly the general concept of having them set so they encourage use is valid—because I believe there is elasticity in long distance.

I think we have demonstrated that. So, therefore, lower prices which encourage higher volume are beneficial to us. The answer is, yes, in that regard.

Mr. Flanagan. I basically agree that our answer is almost an unqualified yes, the caveat being we need to know where the funds are coming from that are going to somehow produce universal service at the same time that long-distance rates are low.

Mr. Brown. If the question is do we believe in lower long-distance prices, yes, I think that is——

Chairman Packwood. So long as you can have universal service?

Mr. Brown. Yes, certainly.

Mr. Brophy. I would agree with that. We are neutral as to where the source of funds comes from for local service so long as they are adequate funds to support the investment.

Mr. Robinson. We certainly would advocate low prices. I second the notion that if the price gets lower and lower, the profit element does get eaten up. Competition should implement the technology and innovation necessary to lower the prices and consistent with the cost of providing the service that we see there.

That is the element of the price that we want.

Chairman Packwood. If the Congress decides as a matter of social policy that we don't think local telephone rates can go as high as they are otherwise going to go, then we have to find a way to subsidize them, correct?

Mr. McGowan. If you reach a conclusion that everybody's phone has to be subsidized.

Chairman Packwood. Yes, and having reached that conclusion, the question becomes where to get the fund, and then it becomes nothing more than the usual game, wherever we are going to get it, the source from where we are going to get it doesn't want us to get it from them.

Chairman Dingell. With apologies, there is a vote on in the House floor and the Chair will ask Senator Packwood to chair while the House goes to vote.

Chairman Packwood [presiding]. Mr. Flanagan, you are building a teleport, is that right?

Mr. Flanagan. Yes, sir.

Chairman Packwood. You are going to receive the messages by satellite in the teleport and distribute them by fiber optics throughout the business district in Manhattan and in some places in Queens?

Mr. Flanagan. That is correct.

Chairman Packwood. That will make you a total bypasser; right?

Mr. Flanagan. That is true.

Chairman **Packwood**. Charlie, do you think you would have any trouble recognizing him as a bypasser if you saw him in the dark?

Mr. **Brown**. No, I know he is a bypasser.

Chairman **Packwood**. Do you think we would have any difficulty figuring out a fee to levy on him to help pay the cost of long distance?

Mr. **Brown**. Yes, I think we will. I hope I am not the one that has to figure it out. I think anybody is going to have trouble figuring out how he should be taxed for his bypassing.

Chairman **Packwood**. I am more inclined to call it a fee than a tax. If we are inclined to continue the subsidy and include the bypassers, would you just as soon we come up with a system of collecting the fee or would you like to have a hand in planning how we do it?

Mr. **Brown**. I would really not want a hand in that.

Chairman **Packwood**. OK. We will see where we end up.

We will go back to Don Riegle.

Senator **Riegle**. Mr. Chairman, I want to make sure that we have some time for the second panel. And I know some members may have to leave, so I'm happy to yield at this point.

Chairman **Packwood**. I think, although I see Congressman Wyden is here also, if we can let them ask first. They have to vote.

Representative **Wyden**. I thank the Chairman. As always, Oregonians are so considerate of each other, and I appreciate the Chairman's indulgence.

Mr. Gore and I both discussed this morning the unfairness of making senior citizens and small businesses and others pay even though they don't make one single long distance call.

One of you, I think it was Mr. McGowan, told Mr. Gore that he had mischaracterized the costs. Another one of you told me that I should compare phone costs to owning a washing machine.

I want to make it very clear that this member believes that operating and maintaining the universal phone system is very different than other products like washing machines in that the whole depends on the sum of the parts.

You are just not going to have a universal phone system literally unless grandmothers can call their doctors, unless small businesses can call their customers, and until all America is tied together.

The point I want to make to you is I am going to do everything I can in the days ahead to demonstrate to you that not only is it good social policy, but that it is in your long-term financial interests to see it that way.

I know you don't like much of our bill today, but I think you are going to see a lot of evidence in the days ahead that even though you don't like it today, it is in your long-term financial interests.

Like so many of the industry witnesses, you have been talking about targeted subsidies.

I don't want to see us create another welfare state in this country. Are you advocating phone stamps or setting up means tests or all kinds of procedures to emulate programs in this country that already aren't getting the benefits out to those who need them?

What is your position on phone stamps?

Mr. **Brophy**. I think there are many systems already in place where we have means tested entitlements and this could be a means tested entitlement.

I was talking to a high level Government worker the other day who told me that he had a single line phone system and had just purchased a computer and enjoyed going home and talking to the source.

His wife complained because that tied up his phone line, so he subscribed to lifeline service at a minimum charge and he was using that for his $3,000 computer to access the information base at the source.

It is a question of whether a subsidy should go to a person in that situation.

Representative **Wyden**. It shouldn't, but unless you give us specific ideas, not generalizations about targeted subsidies as the way to go, you will go another step toward locking senior citizens and others out of universal phone service, because they will have nothing to do with a system with the stigma of welfare.

They will ignore some of their medical needs and not follow up on calls to the doctors. I think that is a big mistake.

I think you have an obligation to come in here and describe a system that is going to work.

Senator **Riegle**. Would the Congressman yield?

I would like to ask each member of the panel to submit a response in detail as to how they think that might best be done. I mean, we are here to gather professional opinion.

Representative **Wyden**. I thank the gentleman.

Chairman **Packwood**. I agree completely with my colleague from Oregon and with Senator Riegle.

If we are going to go to a means test on the telephone system, with all the telephones that exist in this country, I cannot think of a more difficult means test to administer.

I was going to suggest, unless there are further questions, that we adjourn this panel and move on to the next panel. Mr. Lautenberg.

Senator **Lautenberg**. Let me please look at my notes, Mr. Chairman.

If I might take a minute for a couple of quick questions, or would you prefer to just move ahead to the next panel?

Chairman **Packwood**. Go ahead.

Senator **Lautenberg**. I wanted to ask Mr. McGowan something. You are aware of the proposal submitted by Congressman Markey and the one that I have introduced, which target assistance to the needy.

Let me ask you to discuss the merit of the other approaches for a moment. Do you think that the local telephone companies should be held harmless for as much as 90 percent of the costs that are above 110 percent of the national average?

What does that do to the incentive to become more efficient? Who does that help, and who does it not help?

Mr. **McGowan**. I don't think we know. One of the things we are short on is specific information about the items of cost. I saw where the FCC 2 days ago accepted a suggestion by the State of Michigan to undertake a study to determine the impact of their decision on various States and local service rates. This should help us find out some of that information.

Mr. Brown made a point before that there is quite a variation around the country as to the cost of providing local service, depending upon the age of the plant, the technology, the amount of depreciation and experiences with growth rates.

But I believe that, in terms of any necessary subsidies, we are talking about a fairly modest amount of money, especially considering the size of this industry—a fairly modest amount of money necessary to do the job.

Senator LAUTENBERG. Have you looked at the proposals that are in front of us now, including the legislation that has been proposed by my distinguished chairman's bill?

Mr. McGOWAN. I have. I think they are unworkable and make no sense. I think they are harmful to our economy.

Senator LAUTENBERG. Do you disagree with them then, I take it?

Mr. McGOWAN. I disagree.

Chairman PACKWOOD. I wish you could be more explanatory.

Senator LAUTENBERG. I don't think I want to pursue that further. I think that there is probably some strong sentiment about that.

Thanks very much, Mr. Chairman. I will not keep us any longer.

Chairman PACKWOOD. Senator Riegle?

Senator RIEGLE. One item at this point, Mr. Chairman.

I don't know if the panel is aware, as Mr. Brown presumably would be, but in Michigan we have a limited call lifeline rate system, and a person can get that for $4 a month.

I don't know what your guess would be as to how many people have come forward for that kind of service, but the answer is in excess of 300,000, and I find that a startling number. It prompts me to feel that there is enormous sensitivity here to the economics of phone service.

I would imagine that a lot of people would probably like to have unlimited service or something more than a two-call limit, but they look at it and they are obviously under enough financial pressure that they have opted for this minimal amount of lifeline service.

I am just wondering if that kind of information wouldn't incline you to think that we had better be pretty careful about not pricing basic service up to a point where large numbers of people don't feel they can afford it.

Mr. BROWN. I agree with you. I don't know how much of that 300,000, if that is the number, are in the kind of what we might call abuse category that Mr. Brophy just cited.

Obviously, there is no means test, no targeting with respect to this so I think that would be advisable if, in fact, we are intending to target to the poor, we better do so and not just file a tariff which everybody can use for their own purposes as second line or whatever.

Senator RIEGLE. Coming back from a major State, is that kind of data what you would have expected?

Are you surprised at that?

Mr. McGOWAN. I am surprised at the number, but I probably shouldn't be.

For example, in California where we checked, we found that most of the lifeline service there is connected to ski chalets, and these people want to have a phone for their friends to use to call them—all incoming calls. This service costs $2.50 a month.

But these very same people have an average of something like $18 a month in long distance phone bills.

It is unlimited calling coming in and they have a flat rate line going out. This strikes me as an abuse of the principle involved. If I had a ski chalet, I would have lifeline service, because I don't want to talk to my neighbors. I don't know them.

I want to call long distance. Of your number, I don't know how many would fall into that category.

Senator RIEGLE. It would be useful and I would ask that we try to get more backup data on that because Michigan has had a lifeline system for a long enough period that we could draw some lessons from that as it would apply to requests across the country.

I hope we get to the next panel before long, but I do think that it is essential that we work together and that you folks be as helpful as you can in the process to figure out how we solve this problem of maintaining universal service at an affordable rate.

It is absolutely crucial, and if we don't solve the problem you are going to get hit in the head as hard as anybody else.

It is in the public interest to have an answer, and I think we can devise one, but everybody is going to have to meet in the middle.

Chairman DINGELL. The time of the gentleman has expired. The chairman now recognizes the gentleman from Washingotn State, Mr. Swift.

Representative SWIFT. Thank you, Mr. Chairman. I would like to talk a little bit about bypass.

First, I would like to thank Mr. Brophy for, I think, characterizing what the bill contains accurately, and then raising his concerns with it in a fashion that I think has contributed positively to the discussion and the debate.

Unfortunately, other members of the panel and some of our colleagues in the last hour or so, perhaps because they are unaware of precisely what the bill contains, have mischaracterized what the bypass provision is in this bill.

There have been references to precluding bypass, to outlawing bypass and so forth, and then a whole filigree of subsequent disaster has been described based upon a mischaracterization of what we are doing in the first place.

The bill does not preclude bypass. If we were going to outlaw bypass, we would have said bypass is hereby outlawed.

We have suggested that a decision on a potential bypasser should be made on other economic factors than the access charge that would be under our bill charged to the long distance companies, that their decision should be neutral as far as the access charge is concerned.

In fact, the way the provision is in this version of the legislation it could be set at some rate lower than that, but it can't be set higher than that.

So all the talk about prohibiting bypass, stultifying technological innovation, you are going to be jeopardizing international trade, jeopardizing jobs is all setting up strawmen.

That needs to be said for the record.

The second point is that on Wednesday, FCC adopted a change in its access charge that would for the first time assess users of dedicated private lines to pay toward the cost of local telephone service, and while traffic carried over private lines is not metered, the FCC was still able to assess an equivalent charge based on an estimated amount of traffic.

You all support that. You can't be a little bit pregnant. I realize that bypassers who use their own facilities rather than lines leased from the local telephone company may be hard to track, but it is just a little bit more complexity in the same problem that you have already brought in at one end.

Complex, certainly. Impossible. Nonsense.

Third point. Those who seem terribly concerned about the complexity of the bypass process are extremely glib in talking about telephone welfare, and yet we had testimony yesterday from PUC commissioners who indicated that such a telephone welfare process would be horribly complex and extraordinarily difficult to implement.

You get the complexity on one end or on the other. I am suggesting that our way, the consumer benefits if we deal with the complexities of bypass.

Finally, we heard yesterday that residential bypass is not far away, that technology is coming along that is going to permit residential bypass, and by loading all of this on the residential consumer, you are going to be encouraging bypass at that end, whereas the approach we take in the bill would be neutral in that respect, as well.

Now, I think I have accurately described what the bill does so we can get that on the record and back to talking about what the bill does, not horror stories based upon what it doesn't do.

Then I have made a couple of points which I think are arguable, and I would be happy at this point to cease and desist, and let any of you comment, but please comment on what the bill does, not on what it doesn't do.

Mr. McGowan. If you penalize someone economically for using a technology—whether he uses an available system that he believes is better for him, maybe it gives him higher speeds, or the local phone company doesn't offer it, or for whatever reason—if you penalize him economically, then you are prohibiting him.

If you say, "You can do it, but we charge you so much money, it is not worthwhile for you to do it." Then you can't say you are not precluding use of techology when you economically penalize somebody for using it.

We wanted all of our terminals connected in New York City, and we asked New York Telephone to do that, and they said "No." So we installed our own fiber optics. Fiber runs up and down Manhattan connecting all our terminals together.

New York Telephone would be happy to do it today. They said, "We will never turn you down again."

They want to provide ample phone service and I want them to do it; but in the meantime I had to have capacity up there. You would say that, if I used my own capacity, I would have to pay extra to do so. If I had to pay over and above the cost of building my own system, then the inherent economies of fiber would disappear on me.

Representative SWIFT. You assume that the bypasser gets no benefit out of local telephone service.

Mr. McGOWAN. He does. He gets benefit out of the local power system, the local water system——

Representative SWIFT. You are telling me what is wrong with the bill that doesn't exist in the bill.

You are not responding to the question I asked. Anybody else have any comments?

I yield back the balance of my time.

Chairman DINGELL. The Chair recognizes the gentleman from Colorado, Mr. Wirth, who is the sponsor of the legislation and chairman of the subcommittee.

Representative WIRTH. Thank you, Mr. Chairman.

A couple of comments on your remark, Mr. McGowan, that you thought the first of January would be one of the great nonevent days; is that correct?

Mr. McGOWAN. Yes.

Representative WIRTH. I disagree. There is tremendous potential on the first of January that we might hear some independent statements from local operating companies.

You remember last year when the Yellow Pages issue was up, they were saying it was a wonderful thing that they were losing all the revenue from Yellow Pages and we heard yesterday that the idea of sharing was something that they did not agree with and that they thought it was terrific that all of that common cost be borne in the local rate base, so I look forward to the first of January when we might hear something quite significant and independent from the local operating companies.

We have been waiting for that for a long time.

Mr. McGOWAN. I wasn't here yesterday, but did the Indians from the Grand Canyon show up again?

Representative WIRTH. No, nor did the old lady from Squim. Neither of them made an appearance, but I am sure they will before we are done.

We were talking earlier about consistency, and I think that we on the subcommittee who have been involved in this legislation have always advocated a sharing of costs. That has been a consistent position every since Mr. Van Deerlin was chairman of the subcommittee, that has characterized all the legislation.

There may have been some differences about the level of sharing and the balance between the economic efficiency and the social responsibility goals and how much that sharing should be, but there has always been a position on the subcommittee for sharing.

Let me just ask you, Mr. Brown, if you still stick by the statement that you made last year, when you came down and testified right after the divestiture agreement. You said that upward pressure on telephone rates as a result of today's competitive environment and inflation or not, modified consent decree.

Do you still agree with that?

Mr. BROWN. Yes, sir. I do.

Representative WIRTH. Do you have any comment on the study that has been done which was discussed yesterday by the committee in which we looked at the rationale that was stated in dozens of States for rate increases, and almost all of the rate increase requests, either granted or requests, included reference to AT&T divestiture as one of the reasons for those rate increases.

Now, clearly AT&T at the local level, the States, is saying something very different from what you are saying. How do we reconcile those two statements, the request made in the 50 States and your statement that divestiture is not a contributor to increased rates?

Mr. BROWN. I don't know where the data came from in this chart, but I maintain, and I think the operating companies that were here yesterday maintain that these costs are not due to divestiture.

Representative WIRTH. Mr. Chairman, I don't know if this has been included in the record, but I want to make sure that it is, the study that was done by the Energy and Commerce Committee pointing out that in the States, either granted in 1983 or requests not yet acted upon, how many States the argument has been made that divestiture is one of the reasons for that.

Again, looking for the consistency in all of this, you have told us over the last 1½ that there is no relationship between increased rates and divestiture, that it really is competition and inflation that increases costs and yet a very different message is being given to State public utility commissions and to the public.

I made that point yesterday, and again, would make the point today, which I think you will agree, that divestiture could raise rates, couldn't it, Mr. Brown? If the assets and the debts are improperly allocated between the Bell operating companies and the parent company, that could raise rates, couldn't it?

Mr. BROWN. If the assets were improperly allocated?

Representative WIRTH. Yes.

Mr. BROWN. I don't know. It would depend on how improperly allocated they were.

Representative WIRTH. If you took all the very expensive, recent debt and laid it on the local companies and you walked away with the less expensive long-term debt, and all the newest technology went to AT&T, and the lousiest technology went to the local operating companies and so on, you would end up in a situation where the allocation of the assets in the debt would have a significant impact on local rates, wouldn't they?

Mr. BROWN. I suppose that is correct, but it has nothing to do with actuality.

Representative WIRTH. I am just saying that if the assets are improperly allocated between the parent and the local companies, the local companies will have to raise their rates in order to have the revenues to serve the service area they have historically served; isn't that correct?

Mr. BROWN. If they were improperly allocated on any large scale, I think that might be so.

Representative WIRTH. But if then as you claim that is only a theoretical position, therefore, divestiture should have nothing to do with the increase in rates; is that correct?

Mr. BROWN. That is right.

Representative WIRTH. Then why are so many cases made by the local operating companies that divestiture is the reason for this increase in rates?

All one has to do is read the press and read the rate requests made by the Bell operating companies to the State public utility commissions, as we have done as in the study, to see over and over again that you all are referring to divestiture as one of the major reasons for this dramatic set of rate increases.

Mr. BROWN. Mr. Wirth, I said that divestiture does not have an effect. I said it last year. I have said it all during this year.

I say it now. I believe your exchange with Mr. Staley yesterday said the same thing. I don't know where this data came from, but I maintain my position.

Representative WIRTH. I think the record will show differently. Again, this points out that there are other pieces to the rate-increase puzzle. I have said before and will say again, that whether or not we pass legislation related to access charges and the issue that we have been discussing today, there are significant other variables that relate to the increase in rates. Mr. McGowan talked about one before, the action of the State PUC's. Are they going to grant the total rate increase by the local operating companies, or are they going to be more disciplined as, for example, the State of Florida has been. There are a variety of other variables that go to the rate increases, and we should not fool ourselves to suggest that any actions taken today are going to be totally decisive related to the potential of increased rates. I guess you would all agree with that.

Mr. BROWN. Yes.

Representative WIRTH. It is a pleasure to have you here, gentlemen.

Chairman DINGELL. Mr. Brown, in 1981 you made the statement that over the years, telephone companies have priced their services to support the goal of universal local service. No longer is this policy tenable. More and more we must relate rates to cost, service by service, customer by customer. Do you still believe that setting telephone rates to support universal service is untenable?

Mr. BROWN. I believe it is not tenable to maintain a subsidy of the kind that existed when I evidently said that.

Chairman DINGELL. Mr. Brown, would you identify for us please those classes of bypasses who could not be identified as such?

Mr. BROWN. I am sorry, sir, I do not understand that question.

Chairman DINGELL. Well, everybody says that if we fix the access charges too low or too high, it will encourage particularly if fixed too high, bypassing. Now which users who would be encouraged to bypass by high access charges could not be identified?

Mr. BROWN. Well, I think that there are so many different ways to bypass that it is hard for me to express myself of that subject.

Chairman DINGELL. What category of those persons who would be prompted to bypass by fixing the access charges too high could not be identified by the FCC?

Mr. BROWN. I do not think it is as much a question of identifying them as much as it would be to appropriately charge them for degrees of bypass.

Chairman DINGELL. So all of them could be identified?

Mr. BROWN. I do not know whether all could, but I imagine most of them could by virtue of the plant. The important thing is how much they bypass, not the fact that they have an antenna or they do not, and that I believe is very difficult to determine.

Chairman DINGELL. Most of them who would bypass by wire, would be identifiable unless they had access to some kind of private right-of-way. Those who bypassed by wireless would be identifiable through their licensing process and reports to the FCC, would they not?

Mr. BROWN. I think most of them would, although most people can buy a CB radio without being identified.

Chairman DINGELL. We would identify those folks. CB is regulated and could be regulated differently.

There are some other questions that I find very troublesome. Is the stimulus to bypass a big price increase at a particular place in the communication system?

Mr. BROWN. The stimulus to bypass would be an uneconomic charge caused by subsidy in this situation.

Chairman DINGELL. It need not be occasioned by a subsidy situation. All you would need would be a big cost increase at some place within that communication system.

Mr. BROWN. Bypass is effective when a bypasser can do it more cheaply than a local telephone company.

Chairman DINGELL. That is right, and where the money goes is not really important. What is important is that he finds he can more economically provide that service himself than by going through a conventional system.

Mr. BROWN. Right.

Chairman DINGELL. So if you fix your access charges too high, you would encourage bypass of the local service network, would you not?

Mr. BROWN. I am sorry, I missed the point.

Chairman DINGELL. The FCC's thesis and their recommendations and their plan for access charges is based on the fact that if access charges are fixed too high there will be a point at the entry of the interstate system where bypass by large users will be encouraged, is that not so?

Mr. BROWN. The entry to the local telephone company, yes, or the entry to the customer, yes.

Chairman DINGELL. Now, if you move that point where the charges are going to be so high as to encourage persons to go around the system, you can have bypass occur almost at any point after the point of entry into the local service net. Is that not so?

Mr. BROWN. The bypass is possible to be inserted at any point between the entry to the local company and the customer himself. I understand that, yes.

Chairman DINGELL. Now, you have submitted something very interesting and useful to the committee. In response to a request by Mr. Smith, you have indicated you would submit for the record, and I believe this is most helpful, the different costs to the different States of the FCC's plan.

Could you submit to these committees also, if you please, the cost of the current system that is imposed by pre-FCC regulation and also the costs that would be imposed on the different parts of the communication system by the bill sponsored by Mr. Packwood in the Senate and by Mr. Wirth and I in the House?

Mr. **Brown**. Well, I certainly should be able to give you fairly promptly the current costs, if I understand the question correctly. I don't know how I can determine what the various costs would be on these various bills.

Chairman **Dingell**. Well, these costs were being estimated by Bell witnesses yesterday. If you can't, don't. If you can, it would be appreciated. I am of the view—and I would appreciate it if you would challenge me if you feel that I am wrong—that the overall costs between the FCC's announced plan of regulation, and the plan embodied in the proposal submitted by Mr. Packwood in the Senate, and Mr. Wirth and I in the House and our colleagues, would be exactly the same in the aggregate, is that correct?

Mr. **Brown**. I don't know that they would.

Chairman **Dingell**. Do you have any reason to feel that they would be different?

Mr. **Brown**. I really don't understand, as we have said before, with the difficulty of taxing the bypassers I really don't have any way of understanding what would occur in the way of costs and who would bear them.

Chairman **Dingell**. Perhaps any of your colleagues on the panel could give us a comment on that point.

Mr. **McGowan**. The thing I don't understand, among a number of areas, about what is in your mind, is an apparent subordination of efficiency. Let's take a large company in Detroit that buys hundreds and hundreds of circuits from us. Rather than have Michigan Bell lease its copper wire, it was much more economical to establish a microwave link to that company's building. So we built a terminal there. We, therefore, are not using the copper wire of Michigan Bell. They said it made no sense. We knew it made no sense. So we put a terminal there.

Under these bills, I see somehow or other that large corporations are going to have to pay Michigan Bell for something that they, Michigan Bell, agree doesn't make any sense for them to do.

Chairman **Dingell**. You are making the same point I was making earlier, that is if you fix the access charges too high either at the point where the large user enters the interstate system or too high at the point where the large user enters the local system, the large user is going to find it in its best interest to bypass the system.

Mr. **McGowan**. In that case it made no sense to use local copper cable rather than microwave. It doesn't have anything to do with what you are talking about.

Chairman **Dingell**. So the problem with bypass is not only the problem of bypassing the interstate system; it is a problem of bypassing the local system when you fix the entry charges too high.

Mr. **McGowan**. It has nothing to do with charges. Technologically it makes no sense. There are tens of thousands of tandem tie-line networks in the country today. Users of those networks can't physically tell whether a call they receive originated in the office across the hall, or originated 1,000 miles away.

Chairman DINGELL. If the charges of Michigan Bell are low enough, there is no incentive to bypass the entry point to the Michigan Bell system.

Please let me ask another question, gentlemen. We have heard a great deal about the fund that would be set forth in the legislation that the two committees are considering today, and it has been consistently noted that poor people in low-cost areas would be subsidizing rich people in high-cost areas. But isn't it also true that the fund would require, and more likely require, long-distance customers in low-cost areas, primarily large business users, to support local residential customers in high-cost areas?

Mr. BROWN. If you are asking me, would you repeat the last part of that?

Chairman DINGELL. Isn't it true that the high-cost fund really requires long-distance customers in low-cost areas who are primarily large business customers to support local residential service in high-cost areas?

Mr. BROWN. Yes, sir.

Chairman DINGELL. And that is true between States and within States. For example, in Michigan, we have the Detroit area, which is a relatively low-cost, densely packed service area, and we have the Upper Peninsula of Michigan which is relatively sparsely populated. It would be true that our bill would require people in the Detroit area to provide some assistance to persons in the Upper Peninsula as well as interstate assistance, say between Michigan and New Mexico, is that not so?

Mr. BROWN. I believe that is so. You are talking about statewide rate averaging, and that effect you are talking about does occur.

Chairman DINGELL. Can any of you provide evidence which would indicate to these two committees that there is any difference, in terms of the overall movement of money, under the two bills as opposed to existing law?

Mr. BROWN. Well, for my part, I would have to take a look at the individual figures and compare the two. I cannot do so now.

Chairman DINGELL. So there is really nothing that shows that the flow of funds between States would be different under existing law from what it would be under the legislation proposed by Senator Packwood, Mr. Wirth, and I, is that correct?

Mr. BROWN. I would have to look to determine that. I cannot say one way or the other.

Chairman DINGELL. But no one at this moment can make a statement to the contrary?

Mr. MCGOWAN. I can. The current practice is for the telephone industry to meet together and decide how money is going to be divvied up. There are constant negotiations going on. They call it separations and settlements, and they negotiate continually. I read in the paper that they will modify something so some money is changed as to who gets what.

Independents use either a national schedule, or sit down in negotiations. I know a lot of telephone companies, each of which has a different deal as to how it gets its money. Some get flat payments; some get money one way, some another way; there are thousands of arrangements. There is no such thing as a law that has anything to do with it.

The last time the telephone industry publicly altered this scheme was called the Ozark plan. But they have made thousands of changes since then. Not one regulatory agency has ever looked at any of those changes to approve it or not. And we were never part of that process, and so we are not bound by it. They would like to think we were, but we are not bound by that. We never agreed to give up our moneys to anybody.

I think the fifth amendment establishes that you cannot be forced to give up your property. So the law is no more than the Ozark Plan. And that has to die, because I won't join it. They can't continue to operate that way. The FCC is now changing it by the 78-72 mechanism. We agree that it makes sense to do it that way. So there is no such thing as a law.

Chairman DINGELL. Let's use existing practices. Instead of saying it is done by law—I think I said it was done under law, but that is not important. How would the requirements of the two bills that we consider today change the flow of moneys among States?

Mr. McGOWAN. The bills as they are written today would, I believe, artificially try to maintain a system of funds flow, the magnitude of which you are trying to guess. In addition, the bills put other restrictions on the industry, such as penalizing the use of technology to go directly to customers, and basically, they try artificially to maintain what you envision the past to have been.

Chairman DINGELL. But in all fairness, it cannot be said that either of the bills would significantly change the flow of funds between States from current practices. It can be said that perhaps it would change the flow of money between different categories of users under the FCC's plan, and perhaps a different flow of money between States than one would find under the FCC plan—now, is that not a fact?

Mr. McGOWAN. I gather what you are trying to do is to maintain that flow of moneys as you perceive it.

Chairman DINGELL. To put it another way, essentially what the bill does is essentially attempt to maintain the status quo as regards flow of money between categories of users and areas in the country.

Mr. McGOWAN. There is other mischief besides that.

Chairman DINGELL. But I don't think that we are greatly lacking in success. Would you like to comment?

Mr. McGOWAN. I can't tell, because I never did study that program about shifting moneys around the country. You have to understand, the way the money is flowing now—and Mr. Brophy should comment—it is based on negotiations that goes back and forth. We interconnect with a lot of independents, and I see some of the deals that they have. They're all over the map: Some higher, some lower, some do studies, some do strictly negotiations.

Mr. Brown and Mr. Brophy would be better judges as to how that money flow would happen. Some of the sections of the bill—where, for example, you would have access charges set by the States—would wreak havoc in this industry. The States would want access charges tremendously high. Obviously, the problem is someplace else. Giving authority to the States is harmful to the public and to this industry.

Instead of having the Bell operating companies accelerate their depreciation, which they have got to do, the States would probably lengthen it. That would be terrible for this industry—if you ever gave that responsibility to the States. It is not hard to figure out what the States would like to do with this industry.

Chairman DINGELL. Let me explain the reason for the question. Yesterday, I have heard the most dire predictions about how these two bills would move money, for example, from Michigan or Illinois to Florida or New Mexico or Arizona or California or places like that, and I was concerned that perhaps the predictions were true. And I had the staff try to analyze the situation.

So I ask you gentlemen, who are the best experts in this area who can tell me whether those dire predictions will come true. I discern that you are not able to tell me whether those predictions can be relied on.

Mr. BROWN. I think to the extent that the bills try to maintain the status quo, presumably the same flow would exist as currently exists.

Chairman DINGELL. The same flow as between the last two users and the same flow as between areas of the country.

Mr. BROWN. I understand that is the objective of the bill, and I don't know whether it is achieved or not. Assume it is for a moment. The principle of what we are trying to say is that the status quo cannot be maintained under a competitive environment——

Chairman DINGELL. Let's address the competitive environment which concerns you. As long as we see to it that your companies and all the other companies in the long-distance business are treated equally, competition is not inhibited. If we favor any of you, then competition is inhibited.

Am I correct or incorrect?

Mr. ROBINSON. I would only say that if we are treated equally in terms of what we are getting, your contention is right. If we are not all getting the same things, then we won't be treated equally.

Chairman DINGELL. What I am getting at is if we treat you all alike, we have not impaired the competition between the long-distance carriers; we have simply protected the local systems and the local users, who are a matter of great concern here. And as the next election comes closer, I can guarantee this will become of great concern to all of our colleagues in the House.

If we don't succeed with a reasonable bill now, I suspect that by next year's election time, you will see a lot more interest in this.

Mr. BROPHY. Competition between the long-distance carriers and private systems or the competition between the local network and the bypasser.

Chairman DINGELL. That is exactly why we deal with the bypass question. We deal with the bypass question by imposing bypass charges. This is why I asked Mr. Brown to try and identify categories of potential bypasses who would not be reached by the bill, because if there is anybody that is going to escape I want to know who he is so I can craft a bill net to reach him.

Mr. BROPHY. We have honestly tried to draft language of that sort and it may be our own inadequacies, but to date we have been unable to structure something that we believe would eliminate uncertainty to such a degree that the telephone industry can survive without being exposed to a drastic amount of litigation.

Chairman DINGELL. With some regret, I find that I have exceeded my time. Mr. Brophy, I want you to understand the doors of the members of these committees are open to you.

Mr. BROPHY. I understand.

Chairman DINGELL. If you have concern that somebody could not be reached by the bill, or concerns of any other unfairness that exists in this legislation, I want to know about it quickly, I want you to come to my door right away.

Mr. BROPHY. I tried to outline in my testimony some of the concerns that we have and the legal opinion that we have attached raises some of the legal issues.

Mr. BROWN. If it were feasible to identify the bypassers, I still see the difficulty in identifying how much they are bypassing and therefore how much they should be taxed.

Chairman DINGELL. I am going to ask you to tell me how I do that. I want you to give me criticism of any parts of this bill which you think are inadequate to catch any sinners.

Mr. BROWN. No, sir, I don't regard them as sinners. What I am saying is I don't see any mechanism in the bill which will charge a bypasser with 100,000 circuits of capacity to bypass from a bypasser who has 12 circuits.

Chairman DINGELL. I think you raise a very good point. Would you give us suggestions as to how we address that.

Mr. BROWN. We don't know how to do it.

Chairman PACKWOOD. Let me take a guess as to what will happen then. We will cast out a net, perhaps ineptly because we have no advice as to how to do it, and we will catch some people too severely and others not enough.

But if we catch and charge Mr. McGowan more than we should, I don't think it will take him long to suddenly ferret out exactly how much he should be paying, which would be less than what we charge. And my hunch is if we don't charge him enough, Mr. Brown, you will very quickly be able to advise us why we are not charging him enough. And I cannot help but believe that the competitive system among all of you in that sense is going to work more efficiently after the fact than you think it is before.

Mr. BROWN. We have already experienced our difficulties in explaining why Mr. McGowan isn't paying enough.

Chairman DINGELL. Gentlemen, you have been very patient with the Chair. The Chair observes that Mr. Gore is here. Mr. Gore, the Chair recognizes you.

Representative GORE. Thank you very much, Mr. Chairman.

I want to associate myself with your last line of questions, and also with the comments just made by Chairman Packwood. I think that both of you are right on target, and indeed, if the ground rules are the same for all of these long-distance carriers, then the effect on the competitive environment they enter into will not be affected.

Mr. McGowan, when my time expired during the last round of questions, I was discussing the injustice that I perceive in requiring users of local telephones to pay 100 percent of the joint and common costs for equipment that you also use in your business.

You responded by comparing it to a sewer hookup fee, and I just wanted to note that if there were interstate long-distance sewers, it might be an analogy worth pursuing, but there are not. There are only local seers. How does that analogy fit? It doesn't seem to fit at all, to me.

Mr. McGowan. Can I try the gas system, where you pay a connection charge to get into the gas system. You pay for connection to a power system. MCI opens up a lot of locations every month. We go to the local power company, and they say: "All right, you are 4 miles from our line; here is how much we are going to charge you."

So we then ask for bids from private contractors locally. A lot of times we will stay with the power company. We write them a check. They certainly don't average out, so we will write a check for $8,000. That gets us into the grid. It's analogous to what gets you into the telephone system.

With electric power, a consumer is purchasing electricity. The consumer is not purchasing long-distance electricity or local electricity. He is purchasing electricity.

Mr. McGowan. He is purchasing access to electrical service or he is purchasing access to telephone service.

Representative Gore. No, he is purchasing a fungible commodity, which is electricity. He is not making a choice between long distance or local electricity. All of the electricity goes to the same provider, from which provider the user buys it.

In the case of the distinction between long-distance telephone service and local telephone service, the situation is completely different. You have a monopoly provider in the local area using equipment that is also used by a variety of competitive long-distance providers.

What you are asking, again, is that the joint and common costs of that equipment which you use in the course of your business be allocated 100 percent to the local users, whether they use your service or not. They pay for you.

Mr. McGowan. You make that statement, but it is not true, Congressman. We pay for the use of the local telephone plant, and we continue to pay and we are going to pay after 78-72 is in. We pay, the local phone company for the use of the local telephone plant. It is just that the customer is paying for his access into the system, his——

Representative Gore. You pay only for part of it. You pay for the initial part of it. You do not help to pay for, under the FCC scheme, the local telephone lines and poles and the local facility.

Mr. McGowan. We pay for the local telephone lines and poles that are required to provide even local telephone service. Under the FCC plan, some years down the road—after 5 or 6 years—we won't pay for the last connection from the central office switch out to the customer's location.

Representative Gore. You act as if that is just a negligible item.

Mr. McGowan. No. I am trying to explain the difference. You are making it sound like the entire thing was something that we were walking away from. That is not true at all.

Representative Gore. It is true. You are walking away from all of the points from the central office out to the local telephone——

Mr. McGowan. For the connection to the grid.

Representative Gore. That is right, but you are using those lines.

Mr. McGowan. No, our customers—I don't use anything, you have to understand. I don't do that.

Representative Gore. You are selling the use of those lines.

Mr. McGowan. My customers are the ones that use our service.

Representative Gore. If somebody in New York City wants to call my home town in Carthage, Tenn., and they pay you money to connect that all, you use the local facility in Carthage, Tenn?

Mr. McGowan. Yes, the customer uses it.

Representative Gore. You are selling the use of that.

Mr. McGowan. Absolutely.

Representative Gore. All right. Now, under the current scheme, long-distance providers pay for that. Under the scheme that we are moving toward, unless the Congress acts, the local customers in Carthage, Tenn., are going to have to pay for all of that, whereas they only pay for part of it now. It is a joint and common cost. It is a joint facility.

Mr. McGowan. That is right. There is a shift of about 4 percent of telephone revenues.

Representative Gore. Let me shift gears just briefly, and ask you, Mr. Brown, about the dropoff issue, the customer dropoff issue, the threat to universal service. I have heard discussions of the dropoff levels being insignificant, but it seems to me we are failing to look at the issue in proper perspective.

We have been seeing universal service growing through the years to its current level of about what, 92 percent? What is the figure you use in the country?

Mr. Brown. It just depends on the geography again, but 93 percent, 95 percent.

Representative Gore. Ninety-three to ninety-five percent. Well, there has been a major national effort to raise that level of universal service upward. Do you think we ought to continue to try to raise it upward?

Mr. McGowan. It is certainly our objective to continue to raise it upward. I think we may have reached saturation here, Mr. Gore, but it is to our advantage to have 100 percent, if we could, that is correct.

Representative Gore. Your company deserves, of course, enormous credit for pushing us to the level that we are at now. I mean, you hear this all the time, I am sure, but maybe it would be comforting to hear it more frequently in these hearings. But we do in fact have the best system in the world, and your company deserves the credit for that, and in no way do my criticisms in any way reflect a lack of recognition of that fact.

I think what your company has done is absolutely magnificent, but it is a reversal now. If we are going to accept a 7- or 8- percent dropoff as OK, it is sort of like, you know, just using the unemployment rate to a certain percentage and saying we can't ever get below that. I don't think that ought to be the case.

I think we ought to have a goal of increasing universal service, and yet your own studies indicate that the dropoff is going to increase rather dramatically, at least according to the Perl study, I understand that you are backing over that somewhat now, but the figures indicate that if the rates go up and cross a threshold, as, for example, in Tennessee it has gone from $12.60 to $28 and something, there is every indication that that 92 or 93 percent figure is going to drop rather sharply.

Is that a matter of concern to you?

Mr. **Brown**. It is a matter of concern. I don't believe it is going to happen. Mr. Perl does not believe it is going to happen, and I believe with the waiver of the access charge and the high-cost subsidy, it will not happen.

Representative **Gore**. Mr. Chairman, thank you very much Thank you.

Chairman **Dingell**. The Chair thanks the gentleman. Mr. Bryant, who had to leave, asked me to direct this question to each member of the panel. It is as follows: Do you intend to support the Packwood-Wirth-Dingell bill in the House or in the Senate, with or without modification?

Mr. **McGowan**. If you would strike everything after the enacting clause.

Chairman **Dingell**. I sort of gathered, Mr. McGowan, that you had some limited reservations on this bill. I am glad to hear you express it.

Mr. Flanagan.

Mr. **Flanagan**. Not at this time. It would depend on what ultimately evolves.

Chairman **Dingell**. Mr. Brown?

Mr. **Brown**. I think it is important that modifications be made. We would be glad to help with that.

Chairman **Dingell**. We would be glad to hear your suggestions. Gentlemen, I mean that. Mr. Brophy.

Mr. **Brophy**. Yes, we would surely agree with Mr. Brown that the bills in their current form would create many problems, and if legislation is to be enacted, it does require modification.

Chairman **Dingell**. Mr. Robinson.

Mr. **Robinson**. We can support the bill with modifications, Mr. Chairman.

Chairman **Dingell**. Thank you.

Gentlemen, we have asked hard questions. I am sure you understand we have an issue that our constituents are concerned with very strongly, and as your billings progress, I think you will be more sensitive to their concerns, and as election time comes near I think our colleagues will be more sensitive.

You have been here a long time and you have assisted the committee very well. We thank you for your courtesy and for your very gracious appearance. Gentlemen, thank you all.

The Chair announces the next panel will be a panel composed of the following ladies and gentlemen: Mr. James B. Booe, Mrs. Vita Ostrander, Mr. Sam Simon, Mr. Robert Nichols, Mr. Gene Kimmelman, and Mr. Michael Woody.

Ladies and gentlemen, if you will come forward, please, to the witness table and take your seats, we will proceed with the hearing. Ladies and gentlemen, the committee thanks you for your presence. We also thank you for your patience, which has proven to be substantial. The Chair will request for a start that you commence on your left and on my right, identifying yourselves, and then we will recognize you in appropriate order for your testimony.

STATEMENTS OF JAMES B. BOOE, EXECUTIVE VICE PRESIDENT, COMMUNICATIONS WORKERS OF AMERICA; ROBERT NICHOLS, LEGISLATIVE AND REGULATORY COUNSEL, CONSUMERS UNION; SAM SIMON, EXECUTIVE DIRECTOR, TELECOMMUNICATIONS RESEARCH AND ACCESS CENTER (TRAC); GENE KIMMELMAN, ATTORNEY, PUBLIC CITIZEN'S CONGRESS WATCH; VITA OSTRANDER, VICE PRESIDENT, AMERICAN ASSOCIATION OF RETIRED PERSONS; AND MICHAEL WOODY, DIRECTOR OF TELECOMMUNICATIONS, STATE OF WASHINGTON

Mr. Woody. Mr. Chairman, my name is Michael Woody. I am director of telecommunications for the State of Washington.

Chairman Dingell. Mr. Woody.

Mr. Nichols. Mr. Chairman, my name is Robert Nichols, with Consumers Union.

Mr. Kimmelman. Mr. Chairman, my name is Dean Kimmelman. I am staff attorney with Public Citizen's Congress Watch.

Mr. Simon. My name is Sam Simon, executive director of the Telecommunications Research and Access Center.

Mrs. Ostrander. I am Vita Ostrander, president-elect of the American Association of Retired Persons.

Mr. Booe. I am James Booe, executive vice president of the Communications Workers of America.

Chairman Dingell. I think for the assistance of our reporter, we will suggest that we commence with you, Mr. Woody, and move right across to your right as we go. Mr. Woody, we recognize you. We thank you. We will request that you limit your statement to 5 minutes, and we will insert the entirety of it in the record. You may consider yourself recognized.

Mr. Woody. Mr. Chairman and members of the House and Senate committees, I would like to express my appreciation for the opportunity to testify today on the issue of universal telephone service. My objective is to present a telecommunications manager's perspective on the issues at hand; this viewpoint is seen as one from within the State government of Washington.

Within the State of Washington, the State government is the largest single consumer of telecommunications goods and services. The State provides, on a shared-use basis, a statewide network which offers long-distance services to State agencies and other political subdivisions far below the cost these same services could be purchased directly from the local telephone companies.

There are over 550 agencies, 220 locations and 100,000 users on the network. It includes all State agencies, and most county and city governments, fire districts, port authorities, Indian tribes, school districts, libraries, public utility districts, transit systems, and all community colleges and universities. The net effect of the State's network is that the cost of communications within all levels of government is reduced. The ultimate benefactor is the taxpayer.

In its use of telecommunications goods and services, the State government of Washington shares the concerns and objectives with the private business sector. Namely, we both strive to procure and operate systems that are efficient and cost effective for our users. The State is not unique in how it tries to meet the business requirements of its using agencies.

To date, most network services operate through the local exchange network and the local utility companies. There are some unique requirements, however, which are best provided through what is referred to as bypass techniques. It is the issue of bypass that is my concern.

In some instances, the State is a bypasser of the local switched network. There are some governmental functions where bypass is the normal mode of operation. The State's department of emergency services needs a network in place that can be relied on to function in cases of natural disasters.

For example, when Mount St. Helens violently erupts, the public is advised, through the emergency broadcast system, not to use the public telephone system unless it is absolutely necessary. The public network was not designed to function in these overload or disaster situations. Yet this is the very time that the department of emergency services must function, that it must have the full availability of a network;-and this is why they must bypass the local exchange.

The State's department of natural resources uses private microwave facilities to monitor forest fires within the remote wilderness areas of the State; areas on mountain tops where there are no local exchange facilities. Likewise, the department of transportation has an extensive private microwave system that is used primarily for mobile radio dispatching of highway maintenance and repair vehicles; the department has private circuits installed for remote control of highway weigh station signs and mountain pass signs relaying weather conditions ahead and closure information during the snowy winter months.

The Washington State Patrol uses private mobile radio for law enforcement and has a rather extensive microwave network dedicated to its support. Obviously, many other lifeline-type services, such as 911 dispatching, that use private radio systems as well.

All of these services would fall into the category of bypass under the definitions of the proposed legislation. In providing many public services, governmental functions bypass is an absolute requirement; in providing others, it may only be an economic alternative. Our concern in the bypass issue revolves around the underlying assumption that there is something intrinsically wrong with it.

From a telecommunications manager's perspective, this notion is difficult to reconcile with my perceived essential job function. It is my job to make the network and systems cost effective and efficient; to take advantage of technology and competition by optimizing where economically feasible.

I am concerned that bypass is treated as an undesirable and should, therefore, be discouraged, not encouraged; that this discouragement will affect competition and technological advancement, and ultimately the taxpayers of the State of Washington.

Mr. Chairman and members of the committees, I am neither a lawyer nor an economist nor a policymaker on telecommunications matters within the State of Washington. I am a manager of a large telecommunications network. As a consumer, I can appreciate that the matters before you are extremely complex. They involve technical telecommunications issues and serious matters of public policy that have developed over the past 50 years. The issues involve a grave concern over the rapid rise of local rates and the threat to universal service.

The issues are not simple and neither are the solutions.

I would suggest for your consideration that Congress mandate a comprehensive investigation clarifying some of the gray areas that need further definition—one of these being the issue of bypass. Then, after all the issues are thoroughly examined, with input from all sectors of the telecommunications industry—consumers, providers of service and regulators alike, then proceed with legislation that clearly addresses the major problem areas.

Mr. Chairman and members of the committees, I would like to express my appreciation for the opportunity to share with you some of our concerns on bypass, and would be willing to pursue them further in the question-and-answer session to follow. Thank you very much.

Chairman DINGELL. Mr. Nichols, if you please.

Mr. NICHOLS. Thank you, Mr. Chairman. My name is Robert Nichols. I am legislative and regulatory counsel for Consumers Union. We certainly are appreciative of the opportunity to share our views with you today on this most important topic.

I begin with the observation that has already been made in today's hearing, and that is that the front line in the battle against unreasonable local rate increases is undoubtedly in the public hearing rooms of State public utility commissions. That is where consumers are going to have to fight the biggest fight. Nevertheless, we strongly believe Congress has an important role to play, and strongly support legislation to help preserve affordable telephone service in this country.

In this regard let me make it clear that Consumers Union supports the philosophy behind the bills of both Houses that are being considered today. The discussion which we have in our written comments and some of the suggestions I will make today do not go counter to that philosophy, but rather are suggestions on how that philosophy could be best implemented.

Certainly in the limited time available today I don't have the opportunity to cover all the points which I made in my written comments, but let me try to address three issues.

First of all, what kind of permanent subsidy should we establish so that telephone service will remain affordable for all the people of the United States.

Second, where do we get the money for establishing those subsidies.

Third, what should we do about the FCC's access charge decision.

Let's go back to the first question. It is our strong belief that permanent subsidy mechanisms must be established for the two groups of people in the United States most hard hit by the threatened rate increases. That would be low-income individuals and those people in rural high-cost areas. It is essential that these mechanisms be made permanent, and that they be workable.

Let's deal first with the low-income subsidy. We believe that the Congress should mandate that the States establish lifeline programs in their various jurisdictions, and that those lifeline services meet certain mandatory Federal standards. Those would include, for example, a simple, self-certification procedure—piggybacking on existing eligibility requirements where possible—to direct programs to those in need.

We do not favor cumbersome administrative organizations or programs which would make a welfare program out of this proposal. However, we do think that programs focused on the needy can and should be adopted in all States.

As a second Federal standard, we would argue that the lifeline service should not be permitted to include local measured service provisions. We have a number of problems with the local measured service plans as offered now by phone companies. The elderly in Florida have been very vocal in opposition to measured plans, for example, and we don't think that is the direction to go for lifeline.

What about the States which have a high proportion of their population which might need such a lifeline program? This is where we feel that some part of the universal service fund could be used to subsidize those high costs.

What about rural Americans? It is essential, it is absolutely essential, that as a national policy we establish subsidies which prevent high-cost areas from having local loop costs that greatly exceed the national average. We think that various proposals before the committees can achieve that goal. The important thing, of course, is to make sure that the amount of those subsidies don't overtax those that must pay for them.

This brings me to my second issue, then. The subsidy mechanism has to be funded by someone. Where do we think that should come from? One alternative that has been mentioned in the Dingell and Packwood bills is to push costs on to users of long distance and on a bypassers fee. We think that may work, but it also has some difficulties with implementation that a number of people have talked about in the hearing so far.

We would like to suggest another way of doing it, and that is either to adopt a tax on telephone equipment, or second, to require the FCC to adopt a license fee on transmission capacities. Now, either of these methods is another way to try to reach the problem, and that is to get people who benefit from the use of the local network to support it. We are suggesting that some of the difficulties with usage-sensitive pricing and a fee on bypassers might be eliminated if we go this other route. We have some specific suggestions in our written comments which might be helpful to the committees in this regard.

Third, what should we do about the access charge decision? This order clearly should be overturned, but it also need not be completely junked. Our position on this is that the access costs should be pushed from the residential user to the business user, primarily on the first line of the business user.

Second, that the access charge phase-in period should be extended to something like 15 years rather than——

Chairman PACKWOOD. What is the first line of the business user?

Mr. NICHOLS. Some business users will have several lines coming into their business. Rather than trying to push costs on all those lines, we would put those costs on the initial business line. That is the line with the most inelastic demand. We think the higher fee is appropriate because they benefit the most from that local loop.

By stretching out the transition period and charging business lines more, access fees for residential consumers could start in a range of something like 50 cents, and very slowly rise to a much lower figure than the FCC proposes.

Now, why should we suggest that? Why don't I suggest that we eliminate access charges for everybody? I am concerned, and I think residential consumers are concerned, that we adopt a bill that works, and if we want to adopt a bill that works, we need to address the bypass concern responsibly. We think that if you have a modified access charge plan, funded through an equipment tax or a fee that the FCC places on transmission, and have a targeted but substantial support mechanism for those with low income and the rural areas, you have established the kind of package which will work.

Let me close with this comment. We learned from last year that if the telephone industry substantially opposes a major piece of legislation it is difficult for it to pass. My suggestion is that if modifications along the lines that I am suggesting are made in some of the bills that are before the committees, the telephone industry will be hard pressed to oppose them. That is because it will address their problems with usage charges it will address their problems with bypass, and it will address their concerns about inefficiency. If they then still oppose legislation, we will know where the blame lies; and 1 year from now or 2 years from now, when ratepayers, my constituents and yours, are outraged by what happens, we will be able to pass a far more drastic measure which they won't be able to stop.

Thank you.

Chairman DINGELL. Thank you, Mr. Nichols.

[The statement follows:]

STATEMENT OF ROBERT W. NICHOLS, LEGISLATIVE COUNSEL, WASHINGTON OFFICE, CONSUMERS UNION

Mr. Chairman and Members of the Senate and House Commerce Committees, Consumers Union [1] is very pleased to have this opportunity to address this unusual joint hearing on the vital topic of preserving affordable telephone service in this country.

We commend the members of both committees, and especially Chairmen Packwood, Dingell and Wirth, for their recognition of the importance of this issue and their leadership in pushing for prompt yet rigorous examination of alternative legislative responses.

Consumers Union has been actively representing the interests of residential telephone subscribers in many government forums for many years. We have testified on proposed telephone legislation in the past several Congresses. We filed comments before Judge Greene in the AT&T divestiture case and addressed two Federal Communications Commission (FCC) en banc sessions on the implications of the Bell break-up for residential users. We submitted formal comments in a variety of FCC rulemaking proceedings in recent years including those leading to the FCC access charge decision.[2] In addition, we regularly meet with grassroots consumer groups throughout the country to share perspectives on emerging telephone issues.

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[1] Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide information, education, and counsel about consumer goods and services and the management of the family income. Consumers Union's income is derived solely from the sale of Consumer Reports, its other publications, and films. Expenses of occasional public service efforts may be met, in part, by nonrestrictive, noncommercial grants and fees. In addition to reports on Consumers Union's own product testing, Consumer Reports, with approximately 2.5 million circulation, regularly carries articles on health, product safety, marketplace economics, and legislative, judicial, and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

Consumers Union is particularly pleased with the basic approach toward telephone legislation described by Chairmen Packwood, Dingell and Wirth in their recent press conference. This approach was that: (1) the legislative focus will be on the residential telephone subscriber, particularly those in rural areas and those with low income; and (2) the final version of legislation will assist these groups of subscribers in a manner that minimizes efficiency losses and is pro-competition and pro-innovation. Consumers Union heartily endorses these as the crucial criteria upon which legislation designed to benefit the nation's residential telephone users must be judged.

I. THE THREAT TO AFFORDABLE TELEPHONE SERVICE

Before discussing the elements of a legislative response to the threatened loss of universal phone service it is obviously essential to be clear on exactly what the problem is and, as far as possible, what is causing it. Both Senate and House Committees have held extensive hearings in recent years on the revolutionary changes taking place in the telecommunications field. Much of the information generated in those hearings is pertinent to today's discussion. So are significant events occurring since those hearings: the FCC access charge decision, further developments in the AT&T divestiture proceeding and the recent, dramatically higher local rate filings by the soon-to-be independent Bell Operating Companies. A brief description and analysis of the major forces threatening sharply higher rates follows:

The AT&T Divestiture

The entry of the AT&T consent decree began a fundamental alteration of the structure of the telephone industry. Although the precise impact of the breakup on residential phone rates is far from clear, local companies can be expected to use the divestiture order to buttress pleas for local rate increases. (Indeed they are already doing so in many locations.) Furthermore, some state public utility regulators, who of course have local rate setting authority, have publically states that local rates will rise as a result of the decree.[3]

Consumers Union believes that the divestiture itself is not a legitimate reason for local rate increases and, practically speaking, the breakup is now an issue before state public utility commissions, not Congress.

Consumers Union supported a divestiture of AT&T along functional lines several years before the 1982 court settlement of the U.S. government's cases against AT&T. We viewed such a remedy as essential to make anticompetitive practices which had harmed consumers and retarded competition less likely in the future. We also supported House legislation in last Congress (H.R. 5158) which would have ensured that the breakup was accomplished in a way that local phone companies were fairly treated.

Most observers feel that national legislation altering the terms of the consent decree is now highly improbable. Thus, for all practical purposes, this issue is one solely before state commission considering rate hike justifications. Fortunately, Judge Greene has required several modifications in the original decree[4] which eliminate most, if not all, legitimate grounds for claiming that local ratepayers must pay higher bills because of the divestiture.

Deregulation

A second source of upward pressure on the cost of local phone service comes from a series of deregulatory decisions made by the FCC. The most significant of these permits the use of straight-line, useful life depreciation for telephone company equipment. In many states, this constitutes a significantly more rapid write-off of equipment than is currently allowed by state public utility commissions. This decision has been estimated to boost telephone revenue requirements nationwide—which of course must be reflected in local rates—by $1.4 billion per year.[5]

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[2] MTS and WATS Market Structure, CC Docket No. 78-72, Third Report and Order, 48 Fed. Reg. 10319 (March 11, 1983).

[3] See, e.g., Statements of Edward F. Burke, Rick J. Schneidewind, John Bryson, Joseph P. Cresse and Edward B. Hipp before the Subcommittee on Telecommunications, Consumer Protection and Finance, House Committee on Energy and Commerce. February 2, 1982.

[4] For example, transfer of the Yellow Pages to local companies and requiring AT&T ultimately to bear any costs of network reconfiguration.

Another FCC decision requires the expensing of telephone wiring inside buildings rather than inclusion of such costs in the telephone company rate base. This added another $1.4 billion in revenue requirements last year and should add $2 billion more this year.[6] Finally, rates may also be affected by the deregulation of customer premises equipment—although this issue is still uncertain.

All of these decisions are being phased into effect during the next few years. Each of these decisions is grounded in one or both of two underlying industry trends: (1) rapid technological change which is shortening the useful life of older generation telephone equipment; and, (2) the shift from a regulated monoply environment to one in which competition is increasingly permitted and relied on to "regulate" the market.

Therefore, without necessarily agreeing with all the details of these FCC decisions, one must admit that their principal thrust is probably inevitable. Absent these types of changes the quality of telephone service might suffer and the arrival of a genuinely competitive marketplace—bringing greater consumer choice and lower prices—would be indefinitely postponed.

These deregulation issues lie both in federal and state arenas of interest and responsibility. And some of the bills now before the committees address the depreication issue. However, these bills do not purport to directly determine the substance of depreciation policy but rather the governmental jurisdiction issue—who should set depreciation schedules. However, it is also true that by sending this matter to the state public utility commissions, most of which have been very reluctant to grant useful life depreciation in the past, these bills may in effect be overturning the substance of the FCC depreciation order.

Inflation and Increased Profits

Most industry analysts believe that these two factors plus the FCC depreciation order are the major reasons for local telephone rate increases (but not necessarily the major justifications cited by the phone companies in their filings). Local telephone rates have risen at a pace slower than general inflation over the past few decades. Some companies argue that their allowed rate of return on investment must be increased in order to attract investors and pay for the higher cost of borrowing money today.

Regardless of the merits of these arguments, they clearly lie solely within the jurisdiction and responsibility of the state public utility commissions. As such, no bill now before the committees addresses these factors.

Revised Separations Procedures

It is the almost arcane process called "separations" which determines how to apportion jointly used telephone plant (used by local and long distance calls)—and associated revenues, expenses, etc.—between the two governmental jurisdictions involved: the FCC (long distance) and state utility commissions (local calls).

This is the location of the so-called "subsidy" flowing from long distance revenues to local rates. Consumers Union strongly believes that use of the word "subsidy" is highly misleading. Most jointly used local phone equipment has a fixed cost: it does not vary per call. This means the dollar cost which any one call—local or long distance—imposes on the local network cannot be precisely determined. Thus, in the separations process, regulators must resort to rough, inherently arbitrary approximations when deciding how much revenue from long distance calls should be given to local companies.

This is why the current long distance separations contribution—about 26 percent of the cost of the non-usage-sensitive equipment of local companies—cannot be said to be payment beyond its true economic value, i.e., a subsidy. Since the "true" costs of using local company equipment cannot be determined, the long distance revenue contribution level can hardly be said to exceed that cost. Rather, the long distance contribution is a payment required by the integrated nature of our telephone system and by our federal-state governmental system and is set at a level determined by public policy, not economic costs.

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[5] Washington Post, 2/17/82, pages K-1, 3.

[6] Id.

The Joint Board recently decided to freeze the current separations formula at its current level and after two years move to a gross assignment of 25 percent of joint costs to the federal jurisdiction. By this action they eliminated the use of the so-called "SPF" factor which in a rather arbitrary way served to give greater funds to some states than others. Replacing this procedure is a high cost factor which should direct subsidies more directly to rural areas with genuinely higher costs than average.

The separations issue clearly concerns both federal and state jurisdictions. The local rate impact of the current Joint Board decision is not clear; but the overall percentage of payments from long distance revenues is only slightly reduced. Some states, however, will receive less under the new high cost factor than under the arbitrary "SPF" formula currently in use.

The separations impact on local rates really boils down to a question of how and what degree should rural areas receive a subsidy. Some of the bills before the committees propose a new, much higher level of support. Other proposals are silent on the specific support formula which would be determined by a new Joint-Board type entity. There are several questions of interest in this regard for residential consumers: (1) what is the total amount of the rural subsidy; (2) is the subsidy directed at the genuinely high cost areas; (3) are there incentives built-in for inefficient operation by companies receiving the subsidy; and, (4) how is the subsidy funded—i.e., who pays the bill.

Access Charges

Technically speaking, the FCC access charge decision does not effect local phone rates as such. However, because that order will require all telephone subscribers to pay a new monthly flat fee to local phone companies for long distance access, it will certainly look like a local rate increase to the average consumer.

Prior to any changes made by the FCC on reconsideration of its order, this new charge—beginning at a minimum of $2.00 for residential users and $4.00 for businesses per month—will rise over a period of five to seven years until it covers all of the fixed costs of the local phone network attributed to long distance calls (by the separations formula). If fully implemented today, the subscriber fee would be about $8.00 per month, averaged nationally.

The flat fee is not based on usage: it must be paid every month whether or not a long distance call is made. Long distance users would continue to pay a per-minute charge on their calls. However, these time-based rates will presumably be lower than today because the flat fee will cover the fixed costs of the long distance call.[7] During the transition years, those fixed costs not covered by the subscriber flat fee will be charged to long distance phone companies. These companies, of course, can be expected to pass-on most, if not all, of these carrier access charges to long distance customers through per-minute charges.

What is the rationale for this controversial decision which the FCC admits is a "substantial departure" from historic means of cost recovery? All of the reasons behind this decision relate to how costs of a long distance call are recovered.

Most of the cost of a long distance call, about one-half, lies in what is called the "local loop"—the wires connecting the subscriber's telephone set to the first switching station of the local phone company. The cost of this local loop are fixed: they do not vary with usage. Whether one or a hundred-and-one calls are made, the cost of the local loop to the phone company is the same.

How are these fixed local loop costs recovered today? Herein lies the problem. Phone companies currently employ a usage-based (i.e. by the minute) customer charge to pay for most of the non-usage sensitive costs of the local loop. The effect of this pricing system is that high volume long distance users (particularly businesses) pay many times more than their actual monthly local loop costs, while low volume users pay for only a portion of these fixed costs in their monthly bills.

The current pricing system for the local loop worked reasonable well as long as large volume long distance users had no choice but to pay the local phone company. However, this is no longer entirely true. The advent of new, low-cost microwave and satellite technology has enabled some heavy users of long distance service to construct or lease their own long distance facilities thereby bypassing the local phone network for these calls. This is already occurring in some locations. If large users do bypass the local network, remaining subscribers must necessarily pay higher rates to offset the revenue loss. Thus, widespread bypass would not only hurt local phone companies but also residential subscribers who have no alternative than the local phone company for local communications service.

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[7] Consumers Union supports the State of Vermont request to the FCC to order a reduction in interstate long distance rates following implementation of the access charge decision.

The FCC also pointed out that continuing to "overcharge" users of long distance service is economically inefficient. It inflates the costs of the telecommunications business sector (certainly an industry of growing importance to our economy). This weakens our international trade position, causes consumers to pay higher costs for goods and services, and gives faulty economic signals to investors thus distorting our economy.

Consumers Union opposed the FCC access charge decision on the grounds that the Commission over-reacted to concerns about bypass and economic inefficiency. The evidence developed on these issues was not sufficient to warrant a rapid shift to flat rates access fees on all end users.

However, the FCC's fears concerning bypass and inefficiency are not mere fictions, they are genuine threats. The residential phone subscriber has much to lose if both these issues are not responsibly addressed. The issue thus becomes how to move toward a pricing plan for long distance service that minimizes economic inefficiency and bypass losses while not unduly burdening the low volume user and jeopardizing universal service. Our suggestions on how to accomplish this task in legislation are contained in the following sections of this statement.

The access charge issue concerns both federal and state jurisdictions. Virtually all of the bills before the committees alter or repeal the FCC access charge decision. Most of them choose to ban permanently all flat access fees for businesses and residences. They then choose to continue to recover the cost of the local loop solely through usage-based charges on long distance customers. They address the bypass issue by ordering bypassers to pay fees to local companies. These fees are based in some manner on the costs imposed by the bypasser's connection (direct or indirect) with the local network or, in the case of pure bypassers who do not connect at all with the local network, on the value of the local network serving as a "back-up" system. Criminal penalties for avoiding bypass fees are also created.

Summary of the Local Rate Issue

From the foregoing discussion it is clear that most of the factors threatening to push local telephone rates higher are practically speaking not subject to Congressional action. Rather, they are matters to be dealt with by state public utility commissions.

Rate hike requests based on inflation and a higher rate of return on investments are clearly subject only to state evaluation. The divestiture itself is not a legitimate ground for sharply higher rates and Congress shows little interest in reopening this issue since the demise of H.R. 5158 and S. 898 last Congress.

FCC deregulatory decisions, primarily regarding depreciation, are significant factors in local rate increase proposals. However, these decisions are rooted in the need to update telephone equipment and prepare the marketplace for more competition—both of which are rather well established national policies. The Dingell-Wirth bill does transfer jurisdiction over certain depreciation rates back to state commissions. In practice this may mean companies will be granted much slower write-offs in some states. The factual basis necessary for Congress to make—in effect—such a substantive decision is very sparse. It is also questionable whether residential ratepayers would choose to pay somewhat reduced local rates for the next few years if the tradeoff were to lower the quality phone service and to jeopardize the future viability of local phone companies.

This leaves two important matters as the focus for Congressional involvement: the access charge decision and separations process reform. As discussed above, the separations matter is really an issue of subsidies to high cost rural areas and whether the Joint Board plan is sufficient and fair. The extent of local rate increases in rural areas resulting from the Joint Board plan is not clear. This makes it difficult to estimate how much additional subsidy, if any, is required.

Consumers Union strongly supports legislation designed to ensure that geographic variations in basic telephone rates do change dramatically. It is of great value to all subscribers that rural costs are not so high as to drive people off the network. It is also sound national policy to collect reasonable subsidies to help ensure the continued national character of our telephone network.

To properly implement such a policy Congress should then focus on the following questions: (1) Is the total amount of the subsidy sufficient to achieve the goal without over burdening those who must pay for it? (2) Is the subsidy directed at those rural areas which need support the most? (3) Are there sufficient incentives for subsidy recipients to remain efficient? (4) Is the subsidy collected from those best able to pay in a manner that does not create excessive economic distortions?

The FCC access charge decision is the final issue which is clearly within the power of Congress to address. The practical effect of this decision is to raise the upfront charges which local subscribers must pay to obtain phone service. The order is based on a concern about local network bypass and economic inefficiencies both of which are products of the present method of pricing local loop costs on a usage basis.

The FCC's rapid phase-in of flat access fees is not justified by the evidence. However, any alternate method of pricing the local loop must responsibily address the real issues of bypass and inefficiency or residential subscribers will in the long term be far worse off than under the FCC plan.

In conclusion, the threat to universal phone service can be usefully described as both permanent and transitional. Forces pushing up local rates are a permanent threat to the affordability of phone service for rural consumers and low-income subscribers everywhere. Reliable subsidy mechanisms directed at these groups must be institutionalized on a permanent basis.

For other residential subscribers, the local rate problem is more of a transitional once. Numerous forces tending to drive up local phone costs—mainly deriving from the shift from a monopoly to more competitive industry environment—will all hit the consumer at once. The timing and speed of these rate impacts must be better managed by Congressional action. This can most easily be done by altering the FCC access charge decision.

II. LEGISLATION TO PRESERVE UNIVERSAL SERVICE

Consumers Union strongly supports legislation, like the bills now before the committees, designed to preserve the affordability of telephone service for all Americans. Telecommunications is increasingly important in the daily lives of residential consumers. The dawning Information Age promises an abundance of new services to be distributed over the nation's telephone network. Only if those with low income as well as high, the rural as well as the urban resident can afford to stay hooked into that network will we avoid having what some have called a two-class society: the information rich and the information poor.

Our national economy is also increasingly dependent on telecommunications-related industries. Nearly half our gross national product now comes from this sector. These are growth industries which offer the potential of providing jobs and income for an increasingly large part of our workforce. Many of our nation's successes in world trade come from advances in this field. Clearly, then, the residential subscriber has many reasons to want the telecommunications industry to prosper—reasons beyond interest in seeking local bills stay low.

General Principles for Legislation

To truly benefit the residential telephone subscriber—the goal of all the bills before the committees—legislation must satisfy several tests. First, permanent mechanisms must be created for two target groups of our population: low income and rural subscribers. Second, the transitional forces pushing up-from telephone costs higher during the next decade or so must be ameliorated for all residential subscribers. Third, the subsidy collecting mechanism to fund support for rural and low income consumers must be workable; that is, it must avoid taking money from those it is designed to help, minimize economic inefficiencies and distortions, and be administratively enforceable. Fourth, the legislation taken as a whole must responsibly address network bypass and inefficiency concerns and promote genuine competition and technological innovation.

Specific Elements of Legislation

1. *Universal Service Fund.*—Congress should create a new fund designed to maintain affordable telephone service for low income and rural residents. The account for rural areas should use the basic approach of the Joint Board's plan. The formula for distribution of funds should be closely examined to accomplish the following: (1) ensure that no local company loop costs exceed a reasonable figure, perhaps 155% of the national average; (2) direct most funds to those areas with the most need and not to states whose costs barely exceed the national average; (3) include incentives for efficient operations; (4) keep the total rural subsidy at a reasonable level so as not to overburden those who must pay to support the subsidy.

If the level of support is kept near the range proposed by the Joint Board, a surcharge on long distance usage could be used to fund the rural account without significant distortions or inequities. If a larger level of support is desired or anticipated, funding should come from a telephone equipment tax or fee as discussed below.

For low income residents nationwide, legislation should require states to create low-cost lifeline service offerings which meet minimum federal standards. These standards should include: (1) use of a simple, self-certification procedure based on established national income levels (social security definitions of the poor and near poor or other established welfare program eligibility standards); and, (2) a prohibition on the use of a local measured service plan for lifeline service (except perhaps a per call charge after use of a significant number of free calls per month). States with particularly high proportions of low income residents should be able to recover some of the costs of lifeline service from the Universal Service Fund.

The advantages of this type of Universal Service Fund are obvious. It directs funds to those who most need it and institutionalizes these support mechanisms which are essential to preserving universal phone service in the future.

2. *Enact a Tax or Fee on Telephone Equipment.*—To gather money to support the Universal Service Fund. Congress should adopt a broad based, modest tax on telephone equipment. This approach offers important advantages over placing additional fees on long distance usage and establishing charges for bypassers.

Loading costs on long distance calls and bypassers has several drawbacks. First, except maybe as a transitional approach, it creates substantial economic distortions. It increases costs for all businesses which use telecommunications heavily which will then be passed-on to customers. It also may significantly hinder such firms ability to compete internationally. Second, it lessens the likelihood that rural subscribers will receive new information age services which must necessarily use long distance transmission to reach them. Third, it "taxes" the very people who need to receive subsidies, not fund them. Poor and rural subscribers do not make only local calls; they make a significant number of long distance calls which would be "overpriced" if significant surcharges are added to such usage.

Fourth, a fee scheme for bypassers could create enormous administrative and enforcement difficulties. There are no measurement capabilities in place to even roughly identify and measure bypass traffic. Even sophisticated PBX system—the source of much bypass—cannot determine which calls are local and which are long distance (and thus bypass calls). For so-called "hard-wired" bypass systems which do not connect with the local network at all, there are no devices in place to measure calling. Even if such devices are required, accurate self-reporting is not very likely.

Beyond measurement problems are the definitional difficulties. Just what is "bypass"? Broadly construed it could include short wave radio, cellular radio, electronic mail (ECOM), FAX services and the like. To require these valuable services to pay perhaps a significant additional fee would certainly hamper their development, perhaps their existence. If bypass is more narrowly defined, then some services are artificially advantaged by not being charged. Necessary loop-holes in the bypass definitions would then attract all kinds of services which would attempt to squeeze through the opening. Litigation and regulatory proceedings would be endless.

By contrast, an equipment tax or fee (imposed by the FCC) is much simpler and more effective. There would still be some definitional problems for the FCC but equipment sales or transfers are more easily identifiable than bypassers. Moreover the basis for the tax or fee would be simple—a flat percentage—and not depend, for example, on essentially subjective evaluations of the value of the local network serving as a back-up to bypassers.

If a telephone equipment tax is not politically possible, however, other alternatives are available. The Congress could require the FCC to collect a fee on transmission capabilities with exemptions for points in which only one provider serves. Such a fee would still not be based on usage. It would keep incentives for efficient use of long distance facilities and avoid the other disadvantages with solely usage charges.

3. *Repeal the Access Charge Decision.*—We have now described how to assist the poor and rural residents and how best to fund that support. An additional part of the universal service problem remains to be solved. That is the transitional problem for most residential subscribers, particularly the low volume users.

To address this problem the FCC access charge schedule should be stretched out for approximately fifteen years (from the original five years). Second, more costs should be placed on first lines for business and removed from residential customers. Residential access charges could then be zero or at least a nominal $1.00 or so in the first year of the plan and then very gradually increase.

This approach to access charges, combined with our other suggestions, offers many real advantages. It alleviates the impact of substantial access charges on residential subscribers already feeling other phone cost increases. It places additional costs on only the first business line, the one with the most inelastic demand. It also responsibly recognizes the long term threat of bypass and inefficiency caused by permanent reliance on usage based recovery of fixed costs.

4. *Give FCC Intrastate Toll Jurisdiction.*—This action would ensure that all access charges—interstate and intrastate—would be developed under federal guidelines to limit their impact on residential users. Such a merger of jurisdiction is viewed as inevitable by most industry participants and should be done now.

5. *Establish a Citizens Participation Mechanism.*—Legislation should also contain provisions for meaningful public participation in FCC and Joint Board proceedings. Responsible restrictions on funding for groups wanting to participate were contained in an amendment by Mr. Swift last Congress on H.R. 5158. Adoption of these safeguards should lay to rest any concern about abuse of such a program.

Congress should also seriously consider inclusion of a citizens utility board or other mechanism to better enable residential subscribers to be represented in state public utility commissions where the key rate decisions are made.

III. CONCLUSION

Consumers Union looks forward to providing any assistance possible to members of Congress as they refine the excellent bills before them. Residential telephone subscribers want and need workable responses to the threat to affordable service. All the elements of sound legislation to meet that need are contained in the various proposals before the committees. The suggestions we have made go not to the purpose or general thrust of these bills but to the details of implementation. Prompt Congressional action on these measures will be of enormous benefit to residential telephone users throughout the nation.

Chairman DINGELL. The Chair recognizes Mr. Kimmelman. Mr. Kimmelman, we recognize you under the same 5-minute rule we have been recognizing everybody else.

Mr. KIMMELMAN. Thank you, Mr. Chairman.

Mr. Chairman, Senator Packwood, and members of both committees, I appreciate this opportunity to testify before you today in support of legislation to preserve universal telephone service. Congress Watch is supportive of the goals of both the Packwood and the Wirth-Dingell bills. As you will see from our written statement, we also are concerned about implementation problems, and I would like to associate my comments with those of Mr. Nichols from Consumers Union.

I would like to also add a few other points and present the problem from a little different angle.

What we have here I believe is the problem of a transition from a monopoly to a competitive marketplace, and one of the issues at stake here is who bears the cost of the fixed investment of that public telephone network. We have seen the Federal regulators and a great segment of the industry would like to push a large portion of that cost on residential customers. We do not think that is fair.

It is our belief that all telecommunications users, whether they directly or indirectly benefit from the existence of the public telephone network, should pay to maintain it.

In this transition we have the problem of what universal service means. We all know in general what it used to mean. You got your local service from the telephone company. It was a monopoly. That included the phone, service, and everything else. It is a new era now. Universal service must be updated. It means in basic terms the up-front cost one has to pay to get full service, whether it is buying the telephone or leasing it, the wires, the phone, local service, and this new concept—long-distance access.

It is important that we protect people who will not be able to bear this up-front cost. The people most likely to be injured are both the rural and urban poor, those who live on a modest, fixed income, and residents of high-cost exchanges.

Now I would like to turn to the access charge. We believe the FCC access charge was a wrong-minded decision. That decision, based on cost/causation theory, does not reflect what the telephone network really is. Telephone service is more a public good than a private good.

Everyone benefits from it regardless of whether they use it, and we think everyone should pay for it. Therefore, we advocate alteration in that FCC access charge plan. But we must remember that even elimination of that access charge, $2-$8 per month down the road, possibly plus an intrastate access charge, will not solve the problem of affordable phone service for all Americans. Something else must be done.

We recommend a federally mandated lifeline service, a service that would have very low up-front charges, and free calling over a reasonable spectrum.

We do not want to see a welfare bureaucracy created, and we do not want to see the stigma of embarrassing means testing imposed, but we believe it could be possible to target that program—if the industry itself would come in and cooperate and show how it would be done, and help insulate it politically. Mention was made earlier of the windfall profits tax and the energy assistance program. We know that that money has not been insulated and is not going to the people who need it. If that were to be done for telephones, it must be politically insulated, and we would need the cooperation and support of the telephone industry to get that.

For high-cost areas, it is imperative that they receive a subsidy. We don't believe any area should pay more than 50 percent above the national average for its fixed costs. We believe that that subsidy approach should be steeply tapered so that those with very high costs receive full compensation.

Our concern in raising the money to pay for these various programs is that they not create incentives to stop innovation, stop competition, or create incentives to leave the public network in a way that regulators cannot monitor. We hope that both committees will look carefully at the mechanism that they set up to catch bypass. We believe it is imperative that they do catch bypassers, whether or not they indirectly connect with the network, and we just hope that the method that is used is one that does not stifle innovation, but collects enough money to preserve our public telephone network.

Now, everyone seems to acknowledge that the cost of telephone service is only partially attributable to things that Congress can control. We think it is important that there is recognition of a need for some method to help consumers participate in State and Federal regulatory proceedings.

It is imperative that consumers learn about the issues involved in telecommunications policy and are given an opportunity to organize themselves. We hope the Congress will help in fashioning some mechanism for increased consumer participation

In conclusion, Mr. Chairman, I would like to point out that, as far as we are concerned, the bottom line for consumers is reasonable up-front costs, and maintenance and development of a telephone network that promotes innovation, promotes competition with equitable contributions from all telecommunications users.

Thank you.

Chairman DINGELL. Thank you very much, Mr. Kimmelman.

[The statement follows:]

STATEMENT OF GENE KIMMELMAN, STAFF ATTORNEY, PUBLIC CITIZEN'S CONGRESS WATCH

Mr. Chairman, members of both Committees, my name is Gene Kimmelman, I am a staff attorney with Public Citizen's Congress Watch. Congress Watch is the legislative arm of Public Citizen, the consumer research and advocacy group founded by Ralph Nader in 1971.

I appreciate this opportunity to testify in support of legislation that would preserve affordable telephone service for all Americans, and update the concept of universal service to meet modern communication needs. Despite the growth of competition in the telecommunications industry, the cost of basic telephone service is rising at an alarming rate. It is important that Congress step in to preserve universal telephone service before those hit hardest by rate increases—low/income and rural Americans, plus those who live on a modest, fixed income—are forced to give up their phones.

INTRODUCTION

As strange as it sounds, increased competition and technological advancement in the telecommunications industry are leading to a doubling or tripling of telephone service charges. These extreme price hikes result from industry efforts to maximize profits in response to an inadequately structured federal deregulatory program. Besides the unknown future costs of the Bell System break-up, consumers face an immediate $1.4 billion annual rate hike from accelerated depreciation of phone company assets, and $2 billion cost this year from the expensing of inside wiring.[1] Both of these cost increases result from piecemeal, Federal Communications Commission (FCC) deregulatory/pricing decisions. In addition, telephone companies are increasing their installation charges dramatically and urging consumers to purchase their phones—up-front charges that make telephone hook-up a $100–$200 proposition, even without a deposit.

On top of local rate increases and rising up-front charges, the FCC's access charge decision will require consumers to pay a $2 monthly interstate long distance access charge starting next year.[2] This access charge will rise to approximately $8 per month after six years, and is likely to be matched by a $5 intrastate long distance access charge. The price of long distance access covers the cost of local phone company facilities used to connect long distance calls. These costs, previously charged to the long distance carriers and passed on to consumers in the per/minute price of long distance calling, will now become part of each ratepayer's basic monthly service charge, whether or not the customer makes or receives any long distance calls.

While Congress Watch supports increased competition in the telephone industry, we oppose a price structure that jeopardizes universal telephone service. A competitive marketplace with strong incentives for technological advancement can and should be fostered through public policies that preserve basic telephone services at affordable rates for all consumers. Although Congress cannot control local phone rates, it can protect residential consumers by reducing federally imposed up-front charges, and helping consumers monitor state and federal regulatory proceedings.

I. LEGISLATION TO PRESERVE UNIVERSAL TELEPHONE SERVICE

Congress Watch supports the goals of the Universal Telephone Service Preservation Acts of 1983, S. 1660 and H.R. 3621. Both bills would update the universal service mandate of the Communications Act of 1934, to preserve affordable telephone service for all Americans in a competitive telecommunications marketplace.

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[1] Washington Post, February 14, 1982 at K-1, 3.

[2] See MTS and WATS Market Structure, CC Docket No. 78-72, Phase I, Third Report and Order, 48 Fed. Reg. 10319 (March 11, 1983), as modified under reconsideration, July 27, 1983.

II. REDEFINE UNIVERSAL SERVICE

The move from monopoly to competition in the telecommunications industry has altered the meaning of universal telephone service. Under monopoly conditions, affordable phone service meant reasonable local rates. At that time, local service charges included everything necessary to make and receive phone calls: the telephone, wiring and service connection. Now, with separate pricing of each communications product, affordability means reasonable up-front charges for the basic elements of telephone service: the phone, wiring, local service, and long distance access.

a. Access Charges

S. 1660 and H.R. 3621 would reduce consumers' up-front costs by eliminating the FCC's access charge plan. Recognizing the importance of up-front costs to affordable phone service, both bills require interexchange carriers, rather than end users, to pay local phone companies for the cost of connecting long distance calls.

b. Lifeline and High-Cost Exchange Subsidy

Both bills would also reduce up-front costs through a lifeline rate and subsidies for high-cost telephone exchanges. In areas with rugged terrain, sparse population, or a harsh climate, the cost of providing telephone service is enormous. To maintain affordable phone service throughout the nation, it is appropriate for all telephone users to help defray some of these costs. Similarly, a lifeline rate—with minimal service charges and a reasonable block of free calls—would preserve affordable service for low-income Americans.

III. FINE-TUNING AND IMPLEMENTATION PROBLEMS

a. Usage-Sensitive Pricing

While S. 1660 and H.R. 3621 would reduce the up-front charges that threaten to destroy universal phone service, they may not distribute phone system costs in the best manner available. By placing the cost of access on interexchange carriers, these bills would inflate the per-minute charges for all public network, long distance service. This would give large users of long distance services—particularly businesses—an incentive to bypass the public network and purchase private, market-priced long distance service.

b. Bypass

Although both bills seek to reduce this incentive by requiring bypassers to pay a portion of the public network's costs, it is unclear how phone companies and state or federal regulators will be able to define telephone network bypass (it could range from cellular radio to teleconferencing to Federal Express mailing), and how they will determine who is bypassing the network. A better approach may be to assess a large access charge on commercial entities' first business line, as proposed by Representatives Markey and Luken in H.R. 3647, and a registration surcharge on the purchase or lease of private switching equipment—like private branch exchanges—rather than inflate long distance charges. Replacing high long distance usage charges with large up-front access and equipment surcharges would reduce business users' incentives to bypass the public network.

c. Lifeline Rate

Also, both bills would be improved if their lifeline rate and high-cost exchange subsidy were fine-tuned. To assure affordable telephone service for those with few resources or special needs—low-income, handicapped and elderly Americans—it is necessary to mandate federal standards for lifeline service. To avoid confusion and prevent inconvenient calling patterns, time-of-day and distance pricing should be prohibited for lifeline rates, as in H.R. 3647. Lifeline must be simple and cheap, with a large bundle of free or low-cost calls, so the poor and those with special needs can afford phone service without changing their lifestyle.

It may also be appropriate to limit lifeline eligibility to the poor, near-poor, elderly and disabled, if this can be accomplished without creating a new public bureaucracy or humiliating ratepayers with complicated means-testing procedures. One possible approach would be to limit lifeline eligibility to beneficiaries of federal or state entitlement programs, Social Security, unemployment insurance or other standards established by the States. Also, it may be appropriate to allow States with disproportionate numbers of lifeline-eligible subscribers to receive a lifeline contribution from the subsidy fund, or have the fund subsidize one-half the cost of lifeline service in all exchange areas, as proposed by Senator Lautenberg in S. 1677.

d. High-Cost Exchange Subsidy

The high-cost exchange subsidy should be tailored to help regions with low population density, difficult terrain and weather that destroys telephone equipment at a rapid rate. To reflect the public value of nationwide phone service, it would be appropriate to distribute access charge revenue to high-cost exchanges so their fixed costs per access line do not exceed 150 percent of the national average fixed costs. A steeply tapered subsidy, covering all fixed costs above 175 percent of the national average and a small percentage of costs below 150 percent of the national average, would protect high-cost exchanges without creating a large subsidy program.

IV. ELIMINATE THE FCC'S ACCESS CHARGE PLAN

a. FCC Decision

The FCC's access charge decision was based on the need for an economically efficient telephone industry pricing scheme. Since the equipment used to access long distance carriers costs the same, regardless of usage, it is economically inefficient to pay for access on the basis of telephone usage. The FCC argued that high-volume business users would have an incentive to invest in alternative interstate transmission service, bypassing the public telephone network, if fixed access costs remain priced on the basis of usage. This bypass activity would dramatically reduce local phone company revenue, driving rates up for the remaining customers who must cover the phone company's costs.

While the Commission's goal of industry efficiency is an appropriate one, its method of achieving it does not serve the best interest of consumers. A public telephone network, whose investments were made to serve a monopolistic market, cannot be restructured overnight to reflect an equitable allocation of costs. All telephone users have benefitted from the public network's low service charges—either directly, through lower phone bills, or indirectly, through telephone access to 95 percent of American households—and should therefore contribute to the restructuring of the network. Contrary to FCC reasoning, the costs of interstate access were not caused by consumers, but by an industry moving from monopolistic to competitive conditions. Therefore, it makes no sense to shift costs to consumers who are not responsible for telephone industry restructuring.

The access charge decision is fundamentally flawed in its treatment of telephone service as a private good. Unlike a private good, the cost of telephone service is unrelated to its value to consumers. The value of the phone system to consumers is more related to how many people one can communicate with than it is to the price of the equipment necessary to provide service. Whether cheap or expensive, the telephone is only useful if it can provide the means to communicate with a broad segment of the population. If the FCC's access charge decision is left intact, and current phone company rate requests are accepted by state regulators, basic phone service will become an unaffordable luxury for many Americans. Yet those who give up their phones will not be the only losers; all telephone users lose an important resource with each decline in telephone subscription.

Section 2 of H.R. 3621 appropriately acknowledges the public good attributes of telephone service. The bill would implement this economic theory through a surcharge established under section 225 of the Communications Act of 1934, and mandated lifeline service. The surcharge would be paid by all telecommunications users, on an off the public network, "to achieve equitable treatment of all interexchange carriers and other persons who benefit from the services and facilities of each exchange common carrier . . ." section 4.(b). Section 3 of S. 1660 would distribute fixed public network costs in a similar manner.

c. Potential Value of Customer Access Charge

Despite the public good attributes of phone service, imposition of a customer access charge that does not threaten universal service may be an appropriate pricing technique. So long as the total up-front cost of telephone service is affordable, it matters little to residential consumers whether or not their service bill includes an access charge. If business users, who need at least one line for commercial activity, would pay a large access charge for their first line—part of which would be deductible from their federal tax liability—residential access costs would be dramatically reduced. With a business line access charge of no more than $15-20 a month, and long distance service priced near cost, businesses would have no incentive to bypass the public network. So, unless inflated long distance prices are matched with enforceable bypass charges, total elimination of end user access fees may not be in the best interest of consumers.

V. PROMOTE COMPETITION AND TECHNOLOGICAL DEVELOPMENT

Legislation is needed to unite affordable telephone service with increased competition and technological advancement in the telecommunications industry. Consumers stand to benefit from high-quality, reasonably priced telephone services fostered by competition. While some of the new telephone gadgets are no more than exotic luxury items, new services like home shopping, home banking and computerized health care information will improve personal safety and save consumers time and money. Of course, consumers will only benefit from these services if they can afford the telephone that activates them.

S. 1660 and H.R. 3621 seek to promote technological development without sacrificing affordble service. Both bills would create incentives for technological advancement and efficient investment practices. H.R. 3621 would also promote efficiency through cost-based pricing requirements and a ban on cross-subsidization.

Unfortunately, neither bill details a method of uniting affordable service with technological growth. For example, it is unclear whether section 6.(a) of S. 1660 would thwart the development of new bypass technologies that are cheaper than public network service, or whether section 4.(b) of H.R. 3621 would price new bypass techniques used by non-connecting commercial entities out of the market. So long as all telecommunication users make a reasonable contribution to the public network, there is no need to strangle innovative bypass technologies or restrict competition.

Although one of its stated purposes is the continued development of competition, H.R. 3621's grant of asset depreciation authority to state regulators could reduce the likelihood of future competition in local service. Many local phone company assets, historically kept on the books long past their useful life, must be paid for before a company can afford to invest in state-of-the-art equipment. State regulators, facing strong local presure to keep rates low, may find it easier to stretch the period of asset of recovery rather than uncover inflated rate requests that should not be granted. If this practice becomes prevalent, local exchange viability will depend upon preventing competitors with modern equipment from entering the local market.

VI. PUBLIC PARTICIPATION

"Let us recognize what legislation can—and cannot—do. A bill cannot stop telephone companies from requesting inflated rate hikes. But unreasonable rate increases—like the ones pending today—can otherwise be avoided." (From remarks by Representative Timothy Wirth, New Telecommunications Marketplace Seminar, Washington, D.C., June 14, 1983.)

Whether or not Congress passes telecommunications legislation this year, consumers are likely to face sizable phone rate increases in the near future. With over $5 billion of rate increases requested by local phone companies so far this year,[3] $5 billion of intrastate access charges to be assigned, and the FCC continuing its piecemeal deregulation of the telephone industry, it is clear that consumers need more than the elimination of a $2 per month interstate access charge. Without better knowledge of telecommunications issues and immediate representation before state and federal regulators, consumers will not be able to challenge pending rate requests.

Consumer participation in telephone rate proceedings will only decline as telecommunications issues grow more complicated. With the break-up of the Bell System, implementation of the FCC access charge plan, and continued deregulation of telephone equipment looming on the horizon, it will be impossible for consumers to keep up with industry developments.

a. Clearing a Path For Meaningful Consumer Participation

Congress can help consumers organize themselves, without spending a single tax dollar. A simple requirement that phone companies notify ratepayers about the existence of a self-financed telecommunications consumer advocacy organization, would enable ratepayers to join together and monitor regulatory activities. This ratepayer organization, fully funded by voluntary contributions and democratically organized by its supporters, would be able to develop the expertise necessary to represent consumers before telecommunications policymakers. Without a federal requirement that phone companies notify ratepayers of the possibility of forming this type of organization, it will be impossible for consumers to challenge phone company justifications for substantial rate increases.

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[3] See Telecommunications Reports Bulletin of the National Association of Regulatory Utility Commissioners Center for Communications Management, Inc. compiled as of June 30, 1983.

b. Public Participation Financing

A narrower form of consumer representation would be enhanced if federal funds were available to defray the cost of public participation at FCC proceedings. Although a small number of consumer advocacy groups, including Congress Watch, occasionally participate in FCC proceedings, these groups often lack the resources to challenge the empirical foundation of corporate and government participants' proposals. A recent example of this was consumer groups' efforts to oppose the FCC access charge proposal.[4] If federal money were available to finance the presentation of consumers views "that would not otherwise be presented and which are necessary for a fair disposition of a proceeding" as provided for in H.R. 3647—consumers' interests would be better represented in the regulatory arena.

CONCLUSION

Congress Watch supports the goals of S. 1660 and H.R. 3621. With the cost of basic phone service rising rapidly, it is important that Congress act immediately to preserve affordable service for all Americans. By uniting universal telephone service, increased competition, and technical innovation, with a mechanism for enhanced public participation in the policymaking process, Congress can protect consumers' needs in a competitive telecommunications market.

Chairman DINGELL. Mr. Simon, we are happy to recognize you now. We thank you for your patience.

Mr. SIMON. Chairman Dingell, Chairman Packwood, I am pleased to be here today to testify in support of the substance of S. 1616 and H.R. 3621. Universal telephone service is, of course, a national policy set by the Communications Act of 1934, and one which has been to a large extent achieved today. It is now being threatened by the proposed skyrocketing local rates.

The telephone is an essential utility, no different than light, heat, and water. In modern America it is not reasonable to expect people to be able to live without a telephone. At its last consumer assembly, Consumer Federation of America recognized that "Ready access to telephone service impacts upon the health and welfare of the consumer."

The one single decision most detrimental to the promotion of U.S. telephone service is the most recent FCC access fee decision. That decision is serving as a model for pricing structures throughout the telephone system down to the State and local level. If it is followed down to the local level, one can expect to see in the not too distant future, perhaps by 1990, a flat up-front charge of $24 to $30 a month for what we call the right not to make a telephone call.

It is appropriate in our view to have long distance telephone users pay a share of the nontraffic-sensitive cost of the local telephone system. The testimony we have heard this morning and yesterday would make one believe that every payment from long-distance revenues to the local operating company is in fact a subsidy.

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[4] See Reply Comments of Public Citizen's Congress Watch, Before the FCC, In the Matter of MTS and WATS Market Structure, CC Docket No. 78-72, filed September 15, 1982.

Of course that is not true. Long distance is purchasing from the local exchange a service. That service is local exchange. The question is how much of a payment should there be.

A group of consultants to the Kansas Corp. Commission recently concluded a study in Kansas to determine how the cost should be distributed between local and long-distance services, focusing in particular on the gain received from long distance exchange facility. It was their conclusion that on a theory of sharing the savings enjoyed by long distance, that in fact local ratepayers in Kansas are subsidizing long-distance users.

The FCC access fee decision, of course, is being driven by the fear of bypass of the long-distance system. The solution represented by the FCC access fee decision is to simply reduce the cost of telephone service to large and heavy users. By doing so, the large users lose incentive to bypass.

In the meantime the residential telephone user who has no option other than local phone service ends up paying more and more. It is unfair, I believe, to allow the local company to keep potential bypassers on the public system by taking more money from the residential and small business users.

TRAC agrees, by and large, with the proposal that a system should be devised of assessing companies that do bypass based on principles involving direct or indirect access to local exchanges and the reliance upon the local exchange system for universal service, and as a backup for their own use.

I do have to admit that one is troubled by the dire predictions that we heard this morning of the different telephone companies, and would certainly agree that bypass is perhaps the most troublesome provision.

Chairman DINGELL. Mr. Simon, we thank you for your statement, the entirety of which will be inserted in the record.

[The statement follows:]

STATEMENT OF SAMUEL A. SIMON, EXECUTIVE DIRECTOR, TELECOMMUNICATIONS RESEARCH AND ACTION CENTER

Chairman Dingell, Packwood and Wirth, thank you for the opportunity to once again appear to discuss the urgent need for Federal legislation to assure the continuation of universally available telephone service at reasonable and affordable rates to all Americans.

The Telecommunications Research and Action Center (formerly the National Citizens Committee for Broadcasting) is a non-profit membership organization based in Washington, DC, which is devoted to promoting a diverse and democratic communications system responsive to the public interest.

In the last several years, TRAC has been the foremost consumer voice in the national debate over the future of telecommunications. TRAC's involvement has taken many forms. We have carefully covered the debate in ACCESS, our monthly journal of telecommunications news and comment from a consumer perspective. TRAC has published the immensely successful guidebook for telephone consumers, Reverse the Charges: How to Save Money on Your Phone Bill, which is co-authored by myself and Joseph Waz. The book has been distributed to over a quarter of million Americans recently as a pro-bone offering by the Book-of-the-Month-Club.

In addition to helping consumers make sense of all the changes in the rapidly developing telecommunications marketplace, TRAC has been a strong consumer advocate on national telecommunications issues before the Federal Communications Commission. And this is the fifth opportunity that we have had to appear before committees of Congress on behalf of the consumers' interest.

Today, I am pleased to appear before you to endorse the current effort to pass Federal legislation to help residential telephone users in the United States.

On February of 1982 I testified that:

"The measure of the value of the consent decree and the divestiture of the local operating companies will be how well the goal of increased competition in the various telecommunications industries is achieved, and how consumers are benefitted. Short-term reasonable cost increases to consumers might well be justified by increasing competition, new and better service choices, and lower prices in the long term. The question is whether the settlement agreement is likely to achieve these goals."

At that time, we expressed serious reservations about whether the potential benefits of divestiture would be achieved by the proposed consent decree. We identified a series of provisions in the proposed order which in our view were not in the best interest of assuring healthy and strong operating companies that would serve the consumer public with affordable telephone service.

Judge Green in subsequent orders addressed each of the concerns that we identified, and decided them in favor of the local operating company, and ultimately the residential telephone user. Thus, the Yellow Pages remain with the local operating company, local companies have access to certain patent rights developed with ratepayer monies, operating companies will be able to continue to offer customer premises equipment and the local operating companies have the sole rights to the use of the Bell logo and name.

Despite these pro-consumer actions, and others—such as Judge Green's decision that long-distance companies must shoulder the full cost burden of achieving equal access—there is a general perception that "divestiture" is necessarily going to cause local residential telephone rates to double and triple in the near future. This popularly held perception stems from the reality of the massive rate requests being filed in the various states by the local operating companies. And as well documented by the study conducted by the House Energy and Commerce Committee staff, the reasons given by the companies for the rate increase request almost always cite "divestiture."

"Divestiture" however is getting a bum rap. It is our view that "divestiture" in and of itself does not dictate that local telephone rates double or triple. "Divestiture," the process of splitting up the largest company in the world, is of course going to cost, and in a rate regulated industry, consumers are going to be asked to pay those costs. Someone recently made the analogy of "divestiture" to the process of disassembling and reassembling a 747 while in flight. Thus, while there will be some lost revenues and considerable dislocation costs, which normally would result in some additional costs to customers, the rate increase requests being filed in the states today seem to have no relationship at all to those costs.

CORPORATE SEPARATION ANXIETY

Instead, the rate increase requests being filed in the states appear to be the result of what I call "corporate separation anxiety". It is either that or simple greed.

Take as examples, the rate increase requests filed by Southwest Bell in the various states that it serves. In filings that attribute the need for the rate increases almost exclusively to divestiture, Southwest Bell proceeds to include increases due to accelerated depreciation rates, increased rates of return and "losses of long distance revenues." An examination of the filing made by Southwest Bell in Oklahoma, for example, would indicate that no more than one-third of the $300 million in increased revenues it has requested are even arguably related to the direct consequences of divestiture.

It appears that many of the operating companies are afraid that as stand alone corporations they will not be able to continue to generate the revenues and profits that they did while subsidiaries of AT&T. Consequently, they seem to be attempting to take action now to assure that their early performance will gain them high marks. Unfortunately, this is being proposed to be done on the financial backs of the residential telephone consumer.

The proposed legislation cannot, of course, stop irresponsible or unwarranted rate increase requests filed by anxious operating companies. It can, however, have a calming effect on both the operating companies and the state regulators who are being asked to make quick decisions on those requests. (In Oklahoma, Southwest Bell has stated that it *must* have a decision on each element of its rate increase requests before January 1, 1984, which is clearly not the case with respect to its requested increased profits and depreciation rates.) Passage of Federal legislation will assist state regulators in understanding just what divestiture requires and what other federal telephone related decisions require. Moreover, passage of the proposed legislation will eliminate the one ground cited most often by the operating companies to justify the requested rate increase—the loss of long distance revenues.

UNIVERSAL TELEPHONE SERVICE

Universal telephone service is, of course, a national policy set by the Communications Act of 1934, and one which has been to a large extent achieved. It is now being threatened by the proposed skyrocketing of local rates.

The telephone is an essential utility, no different than light, heat and water. In modern day America it is not reasonable to expect people to be able to live without a telephone. At its last Consumer Assembly, the Consumer Federation of America recognized "that ready access to telephone service impacts upon the health and welfare of the consumer". Without ready access to a telephone, people are denied access to the elaborate and sophisticated emergency services and systems developed in our cities over the last decade. A pay telephone in the hallway is not an adequate substitute for a phone in the home. Those who rely on the phone the most often are not mobile enough to reach a distant pay phone. Moreover, in an emergency, it takes precious life-saving minutes to reach a pay telephone. Finally, many of the social service systems for the elderly and the poor are premised on the ability to reach these individuals by telephone on a daily basis.

Universal telephone service at affordable prices should continue to be the basic premise behind national telecommunications policy. Telephone policy and pricing, moreover, should be designed to promote widespread availability and use of the telephone. Too often we find regulators treating telephone regulation just like electric, water and natural gas regulation. There is a major difference, however. With utilities that consume scarce natural resources, national policy must be to discourage rapid or inefficient use of those resources to encourage their availability over the longest period of time. Each cubic-foot of natural gas consumed represents the use of an irreplaceable natural resource. Not so with the telephone. Telephone usage consumes only time and switching capacity—neither of which is scarce in the same sense as natural fuel resources.

Society in fact benefits by the social and business intercourse made possible by the use of telecommunications. Pricing and regulatory policies, therefore, should not discourage or penalize use of this important medium. Instead, it should be concerned with the most efficient use of the system to assure the broadest availability and greatest exploitation of the benefits of the telephone by all Americans.

FCC ACCESS FEE DECISION

The single decision most detrimental to the promotion of universally available telephone service at reasonable and affordable rates in the past year has been the action by the Federal Communications Commission in its CC Docket No. 78-72, Phase I, MTS and WATS Market Structure.

The access fee decision by itself, even as modified on July 27, 1983, will cause local telephone rates to almost double in the next six years by adding an estimated flat fee of $6.00 per month to each telephone bill by 1990. But the access fee decision is serving as a model for price structuring at the state level. And it is this complete reversal of pricing theory and approach at the federal, state and local levels that accounts for the proposed drastic increases in local telephone services—not divestiture.

The FCC decision is premised on the concept that the end-user is the "cost causer" for all the non-traffic sensitive plant costs associated with bringing a telephone line to the home. Since the cost is not variable, and is incurred regardless of usage, and since by definition the end-user is the "causer," therefore it follows that the end-user must pay all the costs of that line. If this philosophy is followed down to the local office we can expect to see in the near future a flat, monthly fee of about $24 to $27 per month, per customer for the right to have what the FCC calls dial-tone service, but which we call the right not to make a telephone call. Calling is then added on as an "option."

The practical result of this decision is to trickle-down costs from the long distance user to the end user. Historically, long distance revenues have been paid to the local operating companies for the use of the local exchange to switch and deliver long distance calls. There is a widely held belief that payments by the long distance carriers to local companies have been more than they "should" be, and consequently constitute a "subsidy" of local rates. The FCC access fee decision purports to bring an end to this situation by phasing in over time a system that ultimately collects all non-traffic sensitive costs directly from the end-user, with only variable costs recovered from long distance users.

It is appropriate in our view to have long distance users pay a share of the non-traffic sensitive costs of the local telephone system. If long distance companies were required to construct their own local distribution system to deliver their telephone calls to the end user, they would have to include the plant costs in their rates. Instead, they are able to use the already existing local exchange system. The question ought to be whether the savings enjoyed as the result of joint use of local exchange facilities should be shared, or is it appropriate to permit the long distance users to call without paying a share of the non-traffic sensitive local plant.

A group of consultants to the Kansas Corporation Commission—William Melody, Robert Warner, William Mihuc and Richard Gabel—recently concluded a study in Kansas to determine how the costs savings enjoyed as the result of joint use of a local plant by long distance and local callers were being distributed. They found that in Kansas, the vast majority of costs savings went to the long distance user. It was their view that an appropriate allocation of the savings would be to divide them equally among all the uses—local, intrastate and interstate.

It is clear that the decision by the FCC unfairly attributes all the non-traffic sensitive costs to the local operating company. In addition, the decision requires that at the end of the phase-in period, the local operating companies must collect the non-traffic sensitive costs equally from each telephone user—at least with respect to the long distance portion of the non-traffic sensitive costs.

Again, this is an approach that was suggested to the FCC by the industry and which is being used as a model in state proceedings.

If fixed costs must be collected as flat fees from end users, then there ought to be a system of allocation among users that reflects the cost impact on the telephone system of different classes of users. In most localities, for example, a small percentage of the telephone users—often between 4 and 10% account for most of the usage and revenues, between 50 and 70%. It is these users that are potential by-passers and whose needs are generally the greatest with respect to enhanced services.

There can be little dispute, moreover, that it is the largest users with the greatest demand for advanced technologies that determine the character, design and equipment necessary for the local operating companies. The rapid depreciation, for example, of existing equipment and the rapid introduction of sophisticated electronic switching equipment, are attributable to the efforts of the local operating companies to meet the increasing demand by large users for state-of-the-art technology. At a recent conference, for example, the president of the United States Independent Telephone Association (USITA) explained the need for independent telephone companies to replace existing equipment with electronic switching. He said there were three reasons: First, the need to offer enhanced services to customers. Second, the need to measure long distance calling by carrier to assess the carrier's access fee. Third, to offer local measured service.

TRAC believes that pricing policies should reflect the reality of cost causation, and that those users whose uses demand the most sophisticated equipment and system should pay the most. Those whose uses do not—primarily residential and small business, one and two line customers—should not be required to pay for a level of service or for equipment they neither want, need, nor use.

The FCC approach, however, would have the total non-traffic sensitive costs of the local exchange divided equally among all telephone users, each paying a share of those costs. Such a system in our view results in residential and small business user subsidizing the large business and enhanced service user.

BYPASS

The FCC access fee decision with its trickle down theory of cost causation is a derivative of the fear of by-pass of the long distance system by the largest of the telephone users. The concern is that if the cost to a large user for the use of the public telephone system is greater than the cost to build a private system, then the large user will build a private system. If a by-passer builds a private system, then the total revenues that had been paid to the local company will be lost to the public system. Then the rates of all other users must then go up—generating even greater incentive to by-pass.

The solution represented by the FCC access fee decision is to simply reduce the cost of the large user. By doing so, the large user loses the incentive to by-pass. In the meantime, however, the residential telephone user who has no choice for local phone service ends up paying more and more for the use of the system.

By-pass is the most difficult problem facing the industry and the telephone consumer. In a sense, by-pass today merely portends the environment ten years from now when competition will exist for local telephone calling. When technology no longer dictates monopoly regulation of telephone communications, when cellular mobile radio, cable and fiber optics make possible several local telephone companies—who is going to pay for the embedded costs of the existing monopoly?

At first glance, it is hard to discern the public merit of by-pass. It is essentially an act of cost containment by an individual corporation for the benefit of either its customers or its shareholders. Is the benefit reaped by those who profit from by-pass worth the cost of by-pass to the public system? My personal first reaction was probably not. Upon reflection, however, I have been convinced that the potential of by-pass provides an incentive for technological innovation and competition. The telephone company is going to try to provide services to potential by-passers at costs below what it would take the by-passers to do themselves.

It is unfair, however, to allow the local company to keep by-passers on the system by collecting more money from the residential and small business users. Further, it is clear that many by-passers are really not by-passers, they are cheaters, that is, they still leak into the local switched network after "by-passing."

TRAC agrees that there should be a system of assessing companies that by-pass based on principles involving their direct and indirect access to the local exchange, and on their reliance upon the local exchange system for universal service and as a back-up system for their own use. We do not, however, have a final proposal to accomplish this goal. And we do share a concern that any assessment of by-passers be done carefully and in a way to minimize negative impacts on competition and innovation.

LIFE LINE SERVICE

TRAC supports the provisions of the legislation which require states to implement a lifeline service. As indicated previously, telephone service is a necessity of life in modern urban America.

We note that today many companies have the equivalent of lifeline type services. In Washington, DC, for example, there is available "Economy Service" that costs about $2.00 a month, plus $.05 a call. Economy Service is available today in the District of Columbia to all telephone users, yet only a very small percentage of consumers use this option. In part, the reason is that the local operating company does not promote its availability. In general, however, we suspect the reason is that most consumers prefer flat rate unlimited calling service, and such a service is currently priced within the reach of most DC residents.

While we strongly support a lifeline service, we are equally opposed to a lifeline service that is available only to people who meet some form of "means test." We are concerned that the language in both bills referring to "low income" people might suggest that the lifeline service will be limited only to those who submit proof that they meet a means test.

Our opposition to the means test stems from the arbitrary nature of federal welfare standards and the likelihood that any such test will miss many people who deserve and need lifeline but who either are not on welfare or who find disclosure of their welfare status as an invasion of privacy. We don't want the telephone company to have a list of people who by nature of the service they have are classified as "welfare" people.

The most equitable lifeline system in our view is one that is based on rate structure. Lifeline is the concept of providing minimum calling for a very, very minimum price to people unable to pay for regular service. These may be the poor, the elderly or those simply temporarily in financial difficulty. A rate structure that makes use of a lifeline rate after a set number of calls would accomplish this goal. Such a system works, however, only if basic telephone rates are affordable. If local rates double and triple relative to other cost items, then it would be more difficult to adopt the rate design solution to lifeline. But with enactment of the proposed legislation, it is unlikely that basic phone rates will increase to the point when only middle-class Americans can afford unsubsidized basic service.

CONSUMER REPRESENTATION

One item of importance to consumers that is missing from both the proposed bills is a provision for effective consumer involvement in telephone policy. Two suggestions have been made for amendments to the bills in this regard. The first is a provision for reimbursement of public participation in federal and state proceedings. Second is a provision authorizing the creation of a national telecommunications consumer board. TRAC strongly supports adding a provision for both items.

Public Participation

Public participation funding provides for the payment of the cost of participation to representatives of groups traditionally under represented in common carrier proceedings. As someone who has for the past five years worked for consumers on telephone matters, I can personally attest to the absence of effective consumer input into the critical proceedings affecting telephone rates. There have been no more than two or three consumer organizations that have been involved in any of the federal proceedings, and their work has largely consisted of providing testimony or written comments—not the extensive factual and legal analysis and studies necessary to back up their positions.

The history of public participation funding by other agencies such as the Federal Trade Commission has shown that its use has been beneficial to agency decisionmaking and the public interest. Funding of public intervention does not supplant the need for other means of consumer organization and advocacy. Indeed, the experience in Wisconsin has shown that even larger consumer groups often need the help of public participation funding to be effective in a specific rate proceeding.

National Telecommunications Consumer Board

When the House was considering H.R. 5158 last year, Congressmen Markey and Mottl offered an amendment to create a National Consumers Board. That amendment was based on H.R. 5421, the National Telecommunications Consumers Board Acty. Extensive testimony on the NTCB idea was submitted at hearings on February 24, 1982, and is included on pages 580 through 630 of the hearings on H.R. 5158. I ask that the testimony on those pages be incorporated into the current record.

The proposal is for Congress to authorize the creation of a non-for-profit board to represent residential telephone consumers. The model for such an organization exists in Wisconsin and is known as the Citizens Utility Board or CUB. Just recently, the state of Illinois authorized the creation of a state CUB.

The Wisconsin and Illinois CUBs were created by state legislation through the enactment of authorizing legislation. State or geographic CUBs represent residential consumers on electric, telephone, gas and water issues within the state before state regulatory and legislative agencies. What we propose is that Congress create an organization based on the same concept, except that it is subject matter oriented—telecommunications—and would operate nationally.

The legislation submitted last year, and which is equally appropriate this year, proposes that telephone companies—both "exchange" (local) and "interexchange" (toll) carriers periodically include with their customer billings invitations to join the Board. These invitations will inform consumers about the organization and give them the opportunity to become members by payment of a nominal annual membership fee.

Members elect the NTCB Board of Directors who govern the activities of the Board on behalf of consumers. The proposal calls for directors to be elected from different regions of the country. Once elected, the directors must represent the telecommunications interest of their district and of the citizens of the United States.

Once established, the Board will be responsible for participating on the state and federal level in proceedings of importance to residential telephone consumers. In states which have state CUBs, the NTCB can act in a supportive role, providing the state CUBs with added expertise in the field of telecommunications. In states where there is no CUB, the NTCB might choose to intervene periodically or to assist other consumer groups to intervene in important cases.

On the federal level, the NTCB would be a constant participant in the various proceedings important to residential telephone rates. As a watchdog of the new carrier's association, the Central Service Organization and the seven regional operating companies—as a participant in the ongoing FCC proceedings involving long distance rates—as an intervenor on behalf of consumers in important federal litigation—as a resource for information for those policy makers wanting a consumer viewpoint on important issues, the NTCB would be available to effectively represent consumer interests whenever the need would arrive.

We strongly urge Congress to add as an amendment to the pending legislation the substance of the proposal contained in H.R. 5421 last year. A NTCB, if in place today, would be available to assist the consumer throughout the United States to respond effectively to the gigantic rate increases currently being proposed at the state level. It is clear that many, if not most of the proposed rate increase requests are outrageous attempts by the operating companies to take advantage of the atmosphere of crisis generated by the divestiture. There is an urgent need for an effective consumer voice throughout the country today to help explain to consumers what their rights and obligations are and to represent their interests at the state and federal level. Congress could do no more for the residential consumer than authorizing a National Telecommunication Consumer Board and ordering its implementation as expeditiously as possible.

Telecommunications Representation Trust Fund

The cost of consumer participation and establishing NTCB is not great. The NTCB will become totally self-sufficient once it is set up, funded from consumer support and its activities. Public participation funding will need to be authorized each year at levels adequate to assure effective participation. Nevertheless, it would be appropriate for Congress to establish a National Telecommunications Representation Trust Fund to assure the availability of funds for the purpose of establishing NTCB and funding it and other intervenors in federal and state proceedings.

There is available to Congress and the ratepayer a sum of money to estalish such a fund; it is the $100 million in revenues taken in by AT&T in 1978 that exceeded the company's allowable rate of return on investment. In CC Docket No. 79-187, the FCC asked for comments on means of returning the money to the benefit of consumers, including the possibility of making the money available to fund public participation in telecommunications proceedings.

TRAC supports action by Congress to legislate in this area. Establishing a Trust Fund consisting of the $100 million in consumer overcharges and administered by consumer trustees, perhaps through the NYCB, would assure the continued effective representation of consumers in state and federal proceedings on telecommunications.

CONCLUSION

In summary, Chairmen, TRAC strongly supports the passage of legislation to assure universal telephone service affordable for all consumers. We believe the proposals contained in the two bills are reasonable approaches to solving the problem. Reversal in whole or part of the FCC access fee proceeding, a more appropriate allocation of non-traffic sensitive costs to long distance or large business users, recovery from by-passers of appropriate user fees, establishement of lifeline service and authorization of consumer representation and a NTCB in a single bill would represent a dramatic victory for the residential telephone consumer.

Thank you.

Chairman DINGELL. We now recognize Mrs. Ostrander.

Mrs. OSTRANDER. I am Vita Ostrander, president-elect of the American Association of Retired Persons. Our membership in our organization is over 14 million older Americans. I am glad to have the opportunity to present the views of ARP on the two bills, the Universal Telephone Service Act of 1983.

From the outset, I would like to applaud the activities of the two committees in holding these two days of very worthwhile hearings in an effort to devise a workable solution to the dilemma currently faced by telephone consumers.

We are all aware of the fact that the telephone is a basic tool of modern communication. Ready access to a telephone is important for all consumers, but it is particularly important for older consumers who as a group are far more dependent upon the telephone than any other segment of our society.

As a result, for older Americans, the telephone takes on increased importance. The importance cannot be underestimated.

The elderly rely upon the telephone as an indispensable tool in relating to and maintaining contact with the world in virtually every facet of daily endeavor.

Under the provision of the two bills, the responsibility for providing minimum local service at discounted rates for low-income residential customers rests with the State public utility commissions.

Conceivably, we are then left with 51 different interpretations of minimum discounted service and low-income consumers, interpretations which may end up based in part on the resources of the local telephone company. Universality may be a national objective hooked up to widely varying localities.

For that reason, we urge the Congress to provide some guidelines to the States in defining what constitutes minimum phone service.

A variety of lifeline or economy service plans already exist, but which ones truly provide universal service at affordable costs to low-income consumers? We don't really know.

AARP would welcome the opportunity to work with you and Congress in including more specific language in this legislation to define lifeline service.

We are also very concerned that lifeline service may be defined in terms of the resources of the phone company to provide it rather than the access needs of low-income subscribers.

Just as universal service fund moneys collected at the Federal level would be distributed as subsidies to local phone companies incurring above-average costs, it seems to us that some amount of federalism should be used to insure that all low-income consumers receive lifeline service regardless of where they live.

The lifeline service provision of the two bills, if adequately defined and financed, will help assure consumers access to the telephone system. We support this concept, but hasten to add that our support of lifeline service for all consumers should not be misconstrued as support for local measured service plans which oftentimes severely curtail phone use by consumers or price its use beyond reach.

Members of AARP, along with other consumers, have found themselves at a disadvantage in evaluating the rash of rate requests by operating companies, including the proposals to establish local measured service We realize that these are matters outside the purview of this legislation and these committees, but we think the committees could oversee the collection and organization of necessary data better than it can be done at the individual State level.

The following are kind of information or guidance that are necessary.

One, we would like to see a compilation on a State-by-State basis that indicates the present existence, the extent and variety of lifeline or minimum basic telephone service systems in the United States.

Two, we would also ask the two committees involved in these hearings to request that the Congressional Research Service or some other appropriate governmental organization look at the various telephone rate structures in use across the country in order to devise a model rate structure that could be used in the individual States.

This would be a tremendous help to consumers in all the States as they deal with their respective public utility commissions concerning possible changes in telephone rate structures. Such a study would have to be undertaken as soon as possible, since such changes are currently under consideration in many States.

Thank you.

Chairman Dingell. Thank you, Mrs. Ostrander. The committee thanks you for very helpful testimony.

[The statement follows:]

Statement of Vita Ostrander, President Elect, American Association of Retired Persons

INTRODUCTION

Good morning: I am Vita Ostrander, President-elect of the American Association of Retired Persons—a membership organization of over 14 million older Americans. I am glad to have the opportunity to present the views of AARP on H.R. 3621/S. 1660, the Universal Telephone Service Act of 1983. From the outset, I would like to applaud the activities of the House Energy and Commerce Committee and the Senate Commerce, Science, and Transportation Committee in holding these two days of very worthwhile hearings in an effort to devise a workable solution to the dilemma currently faced by telephone consumers.

IMPORTANCE OF THE TELEPHONE TO ELDERLY CONSUMERS

We are all well aware of the fact that the telephone is a basic tool of modern communication. Ready access to a telephone is important for all consumers, but it is particularly important for older consumers who, as a group, are far more dependent upon the telephone than any other segment of our society. As a result, for older Americans, the telephone takes on increased importance.

This importance cannot be underestimated. The elderly rely upon the telephone as an indispensible tool in relating to and maintaining contact with the world in virtually every facet of daily endeavor.

We rely upon it to summon help in an emergency—to call the fire department to report a fire, to notify the police when danger threatens, to request an ambulance. We rely upon it when seeking advice from the doctor, dentist, nurse, hospital, health clinic, and pharmacy. We use it as a means of seeking consolation from the pastor or member of the clergy in times of grief or mental anguish. We rely upon it as a constant companion, providing us with a convenient connection with family and friends. The telephone affords us the opportunity to stay involved and active even when the weather outside is bad. It allows us to "go out for the evening" even though in actuality we chose to stay at home during the evening as the result of the threat of crime. For many elderly the telephone represents the only social contact with the outside community. It can also be used as a shopping tool—to order groceries, to buy new clothes, to call the plumber.

For the elderly who are of limited mobility or are required by illness to stay at home, the telephone takes on even greater importance. It, in essence, becomes the arms and legs for the immobilized elderly.

For the elderly at the lowest ends of the poverty spectrum, the telephone is oftentimes utilized as the most economical means of communicating.

ELDERLY ECONOMIC SITUATION

According to the 1980 census, the elderly population—those 65 years of age and older—grew by 5 million persons in the 10 years since the last census. The elderly now constitute one out of every nine persons. If all persons 55 years of age and older are included, the ratio of the older group to the total population raises to one out of every five persons. Many of those in the 55 ot 65 age group are preparing for retirement, working part-time or retired.

Evidence of deterioration in the elderly's income is apparent. The elderly's poverty rate, under the influence of continuing inflation, rose from a low of 14 percent at the end of 1978 to 15.3 percent as of the end of 1981. Additonally, rates of near-poverty (defined as income within 125 percent of the poverty threshold) among the elderly rose from 23.4 percent to 25.2 percent over the same period. Since so many of the elderly (over 10 percent) are concentrated just above the poverty threshold, a drop in income of less than $20-25 a week would cause the elderly poverty rate to escalate to over 25 percent.

Other statistics demonstrate how economically vulnerable the elderly are relative to the rest of the population. In 1981 the median income of elderly headed households was only $9,905—less than half the median income level of non-elderly households. In addition, while 50.5 percent of elderly headed households had incomes below $10,000, only 18.9 percent of non-elderly headed households were in this income category. Even adding to the elderly's income the value of in-kind benefits they receive cannot change the fact that the elderly, as a group, subsist on relatively low and, in many cases, extremely inadequate incomes.

As to the future, studies done by Data Resources, Inc. (DRI) project that the elderly's share of income relative to that of the non-elderly will decline throughout the remainder of the decade of the 1980's erasing much of the earlier progress. Moreover, if a continuation of current economic trends prompts further cutbacks in government income support programs, the elderly could soon find themselves in an economic situation worse than that which prevailed twenty years ago when over one-third of them lived below the official poverty line.

AARP'S OPPOSITON TO PRECIPITOUS INCREASES IN RATE SERVICE

AARP's opposition to precipitous increases in rate service should be viewed against the following backdrop. At present, we are beginning to classify the elderly as the young elderly (60 to 75) and the frail elderly (75 to 85 years of age). This latter group is the fastest growing segment of the elderly population due to longevity. It is this group that has the least flexibility with income and the group that would be the most adversely impacted by the proposed rate service increases.

AARP is very much concerned about the rate increases for local service being applied for by the local operating companies, primarily because these proposed rates are so large—doubling local rates at the least and quadrupling them in some rural areas. The chairman of the Michigan Public Service Commission recently estimated that for every 100 percent increase in phone rates, 10 percent of the people would actually drop phone service completely. For many of the nation's elderly with incomes below or near the poverty threshold, these increases might will mean widespread drop-off—the giving up of phone service. Such people would simply no longer be able to afford phone service at all.

Such deprivation would of course have its ill side effects: greater isolation of low-income elderly from families, friends from social services, and from their businesses, churches, clubs and others making up their social network. It is conceivable that the end result of such widespread drop-off might well result in the institutionalization of persons having to discontinue their phone service. Should this occur, taxpayers would be adversely affected.

The local operating companies are arguing that such increases in the rates are an inevitable product of AT&T's divestiture. It is AARP's position, that the local operating companies should provide for greater justification for these increases than they have so far provided.

OBSERVATIONS ON UNIVERSALITY AS PROVIDED FOR IN H.R. 3621 AND S. 1660

The proposed Universal Telephone Service Act of 1983 has the laudable intent of preserving the universality of our national telephone system in both geographical coverage and individual access. Unfortunately, it provides for the financial means to achieve universality only for areas whose local telephone systems incur costs more than 15 percent above the national average. The high costs of service to rural and remote areas would be offset by subsidies from the Universal Service Fund, thereby reducing the rates which local companies in those areas would have to charge to generate needed operating revenue. All consumers, including low-income elderly, would benefit from this provision.

But what of the needs of the vast majority of low-income persons who reside not in high-cost rural areas, but rather in low-cost urban centers? Or those families below the poverty threshold who live in rural areas which do not quite qualify for the Fund subsidy? How is universality—defined as individual access to the national phone network—to be preserved for them?

Under the provisions of HR. 3621 and S. 1660, the responsibility for providing minimum local telephone service at discounted rates for low-income residential customers rests with the state public utility commissions. Conceivably, we are then left with 51 different interpretations of minimum, discounted service and low-income consumers—interpretations which may end up based in part on the resources of the lcoal telephone company. Universality may be a national objective hooked up to widely varying locales.

For that reason, we urge the Congress to provide some quidelines to the states in defining what constitutes minimum phone service. A variety of lifeline or economy service plans already exist, but which ones truly provide universal service at affordable costs to low-income consumers? AARP would welcome the opportunity to work with you and the Congress in including more specific language in this legislation to define "lifeline" service.

We are also very concerned that lifeline service may be defined in terms of the resources of the phone company to provide it, rather than on the access needs of low-income subscribers. Just as Universal Service Fund monies collected at the federal level would be distributed as subsidies to local phone companies incurring above-average costs, it seems to us that some amount of federal-level funds should be used to insure that all low.income consumers receive "lifeline" service, regardless of where they live. The funds needed to guarantee universality in this way need not come exclusively from user charges, but could perhaps be drawn from the proceeds of federal excise taxes on phone service and channelled to the states.

The lifeline-service provisions of H.R. 3621/S. 1660—if adequately defined and financed—will help assure consumers' access to the telephone system. We support this concept but hasten to add that our support of lifeline-service for all consumers should not be misconstrued as support for local-measured-service plans which oftentimes severely curtail phone use by consumers or price its use beyond reach.

AARP'S SUPPORT OF H.R. 3611/S. 1660 ON ACCESS CHARGE ISSUE

We are very concerned about the approach taken by the Federal Communications Commission (FCC) on July 27, 1983, when it approved the imposition of access charges which will be borne by consumers. We are thankful that the FCC modified its decision and did not approve a more drastic version of the proposed access charges that would have adversely impacted even more heavily upon consumers. However, the plan approved by the FCC is still an inappropriate response to the funding dilemma currently faced by the local operating companies. In the first place, the imposition of an access charge incurs a financial burden upon all telephone users before the phone is ever picked up. Therefore, it is conceivable that a consumer who never uses the long distance feature would be forced into paying for access to a system that he/she will never use.

The FCC obviously recognizes the fact that the imposition of an access charge will adversely affect many telephone users. This is the obvious reason why, on Wednesday of this week, the FCC made the decision to gradually phase-in its recommended access charges. This phase-in requires telephone consumers to pay an additional $2.00 a month, on top of their local phone bill, beginning in January of 1984, with the access charge rising to $3.00 in 1985 and $4.00 in 1986. It has been estimated by some that after 1986 the access charge could reach more than $7.00 a month. While this may not seem like a great deal of money to some, it does represent a sizeable sum to low income, elderly consumers at the lower end of the poverty spectrum. For these individuals, the imposition of an access charge might well force them into discontinuing phone service altogether.

Rather than arbitrarily imposing access charges as the FCC proposes, AARP feels that the preferable course of action is that proposed by H.R. 3621/S. 1660 which reverses the FCC's decision on imposing access charges, thus prohibiting the imposition of these additional charges upon all consumers.

COMPOSITION OF PROPOSED UNIVERSAL SERVICE FUND BOARD

The House and Senate versions of this legislation differ somewhat in the proposed membership of the Universal Service Fund Board. The Senate bill specifies that the Board will be made up of 5 FCC commissioners and 4 State Commissioners, while the House bill proposes 4 State commissioners and 3 FCC commissioners with Board decisions subject to final approval by the FCC.

We recognize and support the critical role to be played by both the FCC and the state regulatory commissions in the impelementation of this legisltiaon. However, we believe strongly that the State commissioners should comprise the Board majority, given their responsibilities in insuring universal coverage to consumers, and that Board decisions should not be subject to FCC approval.

NEED FOR DATA TO EVALUATE RATE PROPOSALS

Members of AARP, along with other consumers, have found themselves at a disadvantage in evaluating the rash of rate requests by operating companies, including the proposals to establish local measured service. We realize that these are matters outside the purview of this legislation and these committees, but we think the committees could oversee the collection and organization of necessary data better than it can be done at the individual state level.

The following kinds of information or guidance are necessary:

1. As mentioned earlier, we feel there is a need for the Congress to provide to the states a definition of what actually constitutes lifeline service. Such a definition is

essential in order to avert wide disparity in the inevitable varying of lifeline service from state to state;

2. We would like to see a compilation on a state-by-state basis that indicates the present existence, the extent and variety of lifeline or minimum basic telephone service systems in the United States;

3. We would also ask the two committees involved in these hearings to request that the Congressional Research Service, or some other appropriate governmental organization, to look at the various telephone rate structures in use across the country in order to devise a model-rate structure that could then be used in the individual states. This would be a tremendous help to consumers in all of the state as they deal with their respective public utilities commissions concerning possible changes in telephone rate structures. Such a study would have to be undertaken as soon as possible since such changes are currently under consideration in many states.

Chairman DINGELL. Mr. Booe.

Mr. BOOE. Thank you, Mr. Chairman, Senator Packwood, and other survivors from this morning's session.

We in CWA are very encouraged that both Houses of Congress are acting to preserve universal telephone service. To us, the FCC's access charge mechanism, as adopted in December, runs counter to the basic concept of universal service.

We believe that the end user access charge is inappropriate, it is unfair to the small user, and it will be ineffective in preventing bypass of the local network, and we note that even though the FCC did make some changes on Wednesday of this week, we don't believe they satisfactorily deal with the problems, as has been pointed out today.

We support legislation to insure that all of the toll carriers contribute to local exchange service via the universal service fund. We want the bypassers also to be required to pay, since they have the potential of suddenly putting great demands on the network, in the case of bypass facility outages, or bypass traffic volumes that go way beyond their capacity.

We support the provider of last resort concept, to insure that the ordinary telephone customer has a single entity to look to for service and for equipment, and we are certainly not advocating any monopoly situation, nor do we advocate any kind of cross subsidies.

However, our most urgent concern is not dealt with in any of the legislation that we have seen this year, and that is "employee protection," as it has been addressed in previously considered bills. In the current and what we will call "final" round of national bargaining with the Bell System—that is prior to divestiture—we are encountering serious problems that we really didn't expect 1 year ago.

In 1982, we raised several serious concerns with Judge Greene about future bargaining with the Bell units, in view of his rulings on divestiture, and he told us:

> Notwithstanding the separation of the operating companies from the Bell System, there will be no obstacle either to adherence by any of the restructured segments of the Bell System, to the terms of existing agreements, or to their abiding by such memoranda of understanding as may have been or may hereafter be negotiated with the union.

Further, the judge said that the divestiture activities, and I quote again, "do not involve AT&T's labor relations, and more particularly, they have nothing to do with CWA or its relationship with the Bell System."

But that was last year. On July 8 of this year, Judge Greene, in an order, curtailed the unlimited portability of pension rights that Bell employees and our members had previously enjoyed, and now the bargainers, both at AT&T and the local operating companies, are taking a position that the judge has ruled, and that the subject of multiemployer bargaining is prohibited, and pension portability in our industry is prohibited, even as a subject in collective bargaining.

So as a result, we need some kind of employee protection provisions, and the only way we see that they can come is through legislation.

We don't want to delay your consideration on legislation that is as urgently needed as universal telephone service, but we do strongly believe that the Congress should give protection to the telecommunications employees who are adversely affected, not by anything within their control, but by divestiture and deregulation decisions of the FCC and of the Federal court.

As an aside, I would be derelict in my responsibility if I didn't take advantage of this opportunity today, to advise your members of the House and Senate committees that deal with the subject of telecommunications that we are now only 8 days from the expiration of the national contracts that exist between CWA and AT&T and all of its affiliates.

The national negotiations are not going well. The critical issues are employment security, wages, and job pressures, and a great deal of them are traceable to decisions made by the FCC and the Federal courts.

The AT&T and their affiliates have injected give-back issues into the negotiations as a result of the FCC and the Federal court decisions, and this has occurred despite the fact that this industry had a $7.2 billion profit in 1982, and the most recent quarter showed $1.9 billion of profits.

We hope we can avoid a strike, but if one occurs, it will occur at midnight next Saturday night, not tomorrow, but 1 week later on August 6. I hate to have to say it, but the Federal Government will carry some of the share of the responsibility if a ntional telephone strike occurs.

The uncertainties that are raised by divestiture in the FCC decisions have been of grave concern to this organization, CWA, since the beginning. We represent the men and women who work in the industry, and they are very proud that they have helped to make the U.S. telephone system the best one that the world has ever known.

The matter of universal service, along with the many other consumer issues, are of utmost importance to CWA. Our executive board is in fact presently considering and about to adopt as policy a lengthy task force report on many of the problems and issues before your committees. This report will be aggressive in its recommendations for union action, in working to assure affordable, reliable telephone service for every citizen in this country.

We intend to mobilize our members and our organizational resources to assure that we continue to have in this country the kind of telephone service that we deserve and have become used to.

We will furnish the House and the Senate committees with copies of our policy and report for their use once it has been adopted by our board.

I thank you for the opportunity to be here today and present our views and comments.

[The statement follows:]

STATEMENT OF JAMES B. BOOE, EXECUTIVE VICE PRESIDENT, COMMUNICATIONS WORKERS OF AMERICA

Mr. Chairman, we are very encouraged by the House and Senate legislation aimed at the preservation of universal service. We understand that "universal service" is a concept, like "beauty," which has no agreed-on definition. But even "competition" lacks a good definition, especially in the telecommunications business.

We support legislation as the strong message needed by the Federal Communications Commission to maintain the nationwide, near-saturation availability of telephone service. Since 1976, we have been greatly concerned over what we have viewed as social experimentation at the FCC which would inevitably lead to the reduced availability of the telephone and far-higher rates to those who remain on the network. We have consistently urged the Congress to establish a modern policy to direct the FCC in its efforts.

We remember the Commission said its Docket 78-72 access charge decision of last December 22 would help keep universal service through the high-cost fund, avoid uneconomic bypass of the network, provide for a quick-response monitoring system and do many other desirable things. Unfortunately, we find it difficult to agree with some of the workings of that access charge mechanism. For example, consider the end-user charge for interstate access, starting at $2 and going up to about $9; while end-user charges would be going up, the "carriers' carrier" charges levied on interexchange carriers would be dropping. We and many others believed that approach was entirely unfair. We also see a flaw in the logic that the new 78-72 access charge discourages bypass. When the access charge per line goes up, we can see the telecommunications managers of large corporate users analyzing the situation and concluding that their companies should have significantly fewer network access lines and far more bypass capability.

From the design of the Universal Service Fund in the FCC access charge decision, we see only limited subsidy of local telephone rates; today the reasonable rates we now enjoy are supported by contributions from toll revenues, through the separations-settlements and division of revenues processes. And the local ratepayer may not be grateful to the FCC for its helping to create the contrived form of intercity toll competition that is leading to the abolition of the subsidies which have over the years contributed to the high degree of telephone service penetration in the United States. Twenty years from now, your successors in the Congress may legitimately question the sanity of the makers of telecommunications policy in the 1970's and 1980's.

Your legislation would instruct the FCC on the end-user charge and provide for a much more adequate Universal Service Fund. It would ensure that the inter-exchange—or interLATA—common carriers would pay the local exchange carriers for the labor- and capital-intensive local distribution facilities necessary for end-to-end service. Your legislation must allow the local exchange to receive revenues when a bypass is effected. Although some claim bypassers would be unfairly treated, we point to a clear enough analogue in the electric power industry. Large users of electricity commonly pay "demand" charges on top of regular usage charges. The rationale is that the electric utility must have extra capacity to accommodate surges of demand.

The telecommunications bypasser will rely on the public switched network in many instances, and with great unpredictability. This bypasser, being a larger corporate user, will be very unsympathetic if the network lacks capacity for sizeable and sudden demands. This lack of sympathy will, as usual, be expressed before regulatory agencies and courts. Thus bypassers ought to be required to pay some form of "demand" charges to cover the costs of the "fallback" network, which is in effect the "last resort."

We see the FCC's action this week aimed at preventing legislation; it may give opponents a fairly persuasive argument against acting at this time. Without legislation, nothing is to prevent the Commission from "re-adjusting" end-user access charge and taking other anticonsumer actions, all in the interests of supposedly furthering competition. We urge you that not be dissuaded in pressing for this legislation. The FCC need not start out from the beginning to comply with the access charge provisions of the proposed legislation. The Commission's work to date certainly can be used to prepare a new access charge mechanism, as an adaptation of what it has planned to do.

We also support the "provider of last resort" requirement, to ensure that the potential user has at least a single source of service and necessary wiring and equipment. We are not advocating monopoly either through the front or back doors; equipment and wiring can be competitively supplied. But we must remember that competitors are quite free to elect not to serve in any given area. Since a telephone company is legally franchised to be the sole service provider in a given area, we believe the cause of universal service is advanced by letting the ordinary user have a full service option. Your prohibition of cross-subsidy will adequately protect against improper revenue flows from regulated operations.

The coming AT&T divestiture points to several areas in which legislation would be useful, from the standpoint of CWA. Interpretations of, and decisions flowing from, the Plan of Reorganization have led to many difficult and entirely unforeseen problems in the reassignments of our members throughout AT&T. Some form of employee protection provisions, modeled on those in previously considered bills, would appear to be in order.

Judge Harold Greene's recent order tentatively approving the Plan of Reorganization has caused the union-represented employees in AT&T two severe problems. One is that the portability of service pensions will exist only for a year after divestiture; the other problem is that we are precluded from bargaining on an integrated basis on pensions. The Judge has ordered that AT&T and the BOCs utilize nine separate pension funds after divestiture. We need remedial legislation—specifically to allow multi-employer bargaining in this unique case—as the only recourse. While the Judge has written in numerous documents that he did not intend to inflict any harm on the employees of AT&T and its affiliates, we believe that the restrictions imposed on our bargaining are denying our union the ability to secure the best possible benefits for our members.

One final item we would like to see in the legislation is trade reciprocity. We recall the energetic activities of the Japanese agents in March 1982, which led to dropping such provisions from H.R. 5158. We expect Nippon Telegraph & Telephone Public Corporation to continue its dissembling and refusal to buy more than puny token amounts of our splendid American telecommunicaitons goods, as the Japanese continue their "protect Japan" program.

Perhaps these other items we consider desirable may have to be attached to some other legislation, in order to keep the Universal Service legislation narrowly enough focused to secure enactment; we recognize that you and your colleagues are facing some massive opposition. We hope the Congress will seize its opportunity to act while there is time. If the FCC gets its access charge mechanism in place, we do not see any turning back.

As Chairmen Packwood and Dingell make clear last week at the press conference, the Senate and House bills are consistent in aim. We believe that the less detailed Senate bill, S. 1660, might be viewed by the Commission as a legislative statement of what already is being done. We suggest more detailed guidance, such as that in H.R. 3621, is more in order. The Commission then will have little doubt as to the intentions of the 98th Congress.

Chairman DINGELL. Mr. Booe, the committee thanks you for your very fine statement. We appreciate your assistance to us.

The Chair recognizes my good friend and cochairman, Senator Packwood.

Chairman PACKWOOD. Thank you, Mr. Chairman. I have only one question of one of the panelists, and, Mr. Woody, that is of you.

In your statement, you say, "Our concern in the bypass issue revolves around the underlying assumption that there is something intrinsically wrong with it."

At least speaking for myself and Chairman Dingell, I know that we think there is nothing wrong with bypass. It is not immoral.

I thought Western Union's undertaking with its teleport and optic fibers is a marvelous system. We are saying that it ought to pay proportionate costs of supporting local rates.

I am curious if your position representing the State of Washington is that you are opposed to our charging bypassers a fee, including the State of Washington, or whether your objection is simply that municipalities, including the State of Washington, should not be charged, but it is all right to charge other private bypassers.

Mr. WOODY. We are not opposed to the imposition of a fee or a fine. My purpose in being here today, Senator, is merely to explain to you the effect of that imposition upon the taxpayers of the State of Washington, that it will affect the rates of our network, and to envision a hypothetical taxpayer in the State of Washington, let me explain to you how our system would affect that hypothetical taxpayer.

Chairman PACKWOOD. I don't mind if you explain, but I don't need any further answer to my question.

I just want to make sure you weren't opposed to charging Western Union if they attempt to bypass the system. I think you may make a good case for exempting municipalities, I don't know, but that is your position basically, that if we tax you, you pass it on to the taxpayers and nothing much is gained anyway.

Mr. WOODY. That is correct.

Chairman PACKWOOD. I have no other questions, Mr. Chairman.

Chairman DINGELL. The Chair thanks the gentleman.

The Chair now recognizes the gentleman from Massachusetts, Mr. Markey.

Representative MARKEY. Thank you, Mr. Chairman.

Mr. Nichols, in your prepared testimony you advocated a five-point approach to telephone legislation.

First, the adoption of the joint board plan for rural subsidy matched with a needs tested subsidy for the poor and the near poor.

Second, you advocate raising revenues from broadly based sources and those off the network.

Third, you stretch out the access charges and decrease its burden on residential consumers.

Fourth, you give the FCC toll jurisdiction.

Fifth, you establish public participation mechanisms.

Is there some reason why that sounds very, very familiar to me? Is that the same approach that is taken in the bill that Mr. Luken and I have introduced?

Mr. NICHOLS. Substantially the same approach, Mr. Markey. I think it is also substantially the same approach that the other bills that are before this committee are trying to take.

My point in my oral testimony was only that the residential users want to get a responsible bill into law and that the suggestions we made are the best way to do that. I think many of the concepts in your bill are among the best to achieve our goal.

Representative MARKEY. So your recommendations do closely parallel the items in my bill?

Mr. NICHOLS. They do.

Representative MARKEY. Thank you.

Mr. Kimmelman, you have suggested many fine-tuning measures or changes needed to improve H.R. 3621, the Wirth-Dingell bill. Do you think that the bill that Mr. Luken and I have introduced incorporates some of these changes? Do your recommendations for changes in the Dingell-Wirth bill exist in a freestanding form in our bill?

Mr. **Kimmelman**. I think some of them do. I think they really need to be combined, because I think the purposes are the same.

For example, in the lifeline area, we are concerned about targeting. We don't think anyone should go forward with that suggestion until we get cooperation from the industry and make sure that it would be politically insulated.

Part of my concern would be to expand that targeting a bit beyond the entitlement programs that you have enumerated in your bill. But, yes, our concerns are basically that any method of collecting revenue to support the public network would be reasonable if it does not overcharge usage, and deter innovation and competition, and that it be policeable and provide assurances that bypassers do not escape and therefore avoid contributing to the network.

So I think really a combination of some of the provisions in your bill with the Wirth-Dingell bill may be the best solution.

Representative **Markey**. Thank you.

Mr. Simon, you spoke of support for a CUB, for a Telecommunications Citizens Utility Board. Last year we lost a tough vote in the subcommittee by an 8-to-5 margin. I intend to bring back CUB for markup in any common carrier legislation.

I have my reasons. The need for CUB is stronger now than ever before.

Do you believe that that is the case, that in fact the changes and disruption in the industry only point out the need to have some kind of citizen participation in the regulatory process?

Mr. **Simon**. Congressman Markey, I think the answer is clearly yes, and I would refer you to the fine study done by the subcommittee staff on the kinds of outrageous and unreasonable rate increase requests being filed on the State levels. These rate increase requests have absolutely nothing to do with the reality of cost or events in the industry; yet, the companies have proposed doubling and tripling in some places.

The only real true response to that is to have an effective consumer voice available at the State and Federal level, and the CUB can do that.

Representative **Markey**. Thank you.

Chairman **Dingell**. The Chair thanks the gentleman.

The Chair recognizes the gentleman from Washington, Mr. Swift.

Representative **Swift**. Just on the very last discussion, I felt all along that the access charge decision of the FCC might not have looked the way it did had consumers been part of the process. They stuck it all on the people who weren't there to represent themselves. And I assume if the long-distance companies hadn't been there, they might pile the access charge on them.

You resolve the problem by doing all the unpleasant things to the people that are not there to represent themselves.

Mr. Woody, you and I have some very similar scars from some battles lost in the past, but I must take issue, as did Senator Packwood, with the idea that we feel there is something intrinsically wrong with bypass, that the bill treats it as undesirable, or discourages it. If that is what you believe the bill does or is our intent, I want to assure you it is not.

We very clearly do not want to discourage bypass. What we are trying to do is to make an agency's decision as to whether to bypass or not have nothing whatever to do with the access charge that would be paid by long-distance carriers.

It should be neutral in that regard, and you listed a whole series of activities that State government might engage in that would make them want to bypass anyway, having emergency services available and so forth, and it is terribly important to understand that whatever your problems may be with bypass, and it is a complex issue and it needs to be worked through, no one is trying to discourage bypass or establish a national policy to do that.

If that is misunderstood, then a whole filigree of other things are assumed, and we get horror stories and a whole lot of stuff that is just irrelevant to what it is we are trying to propose.

Now, the question as to whether government, States, municipalities should be required to pay a fee for bypass or not, let's examine that.

I don't know whether you know this, but approximately how many telephone lines are in the State of Washington? Do you have any idea on that at all? I don't.

Mr. WOODY. We have around 22,000 centrex lines.

Representative SWIFT. That is the State?

Mr. WOODY. Yes, that is the State government.

Representative SWIFT. I am talking about the whole State of Washington.

Mr. WOODY. I would have no idea.

Representative SWIFT. I don't either, but if you take a national average of what the access fee is going to cost, it is going to be 8 bucks a month for every one of those lines for the citizens of the State of Washington, $96 a year times all of those.

It seems to me that whatever bypass fee the State might have to pay, it is going to be infinitely smaller than $96 per line, per customer per year, so that a tradeoff is enormously in favor of the consumer, even if the State's expenses go up a little bit, because they would pay a fee to make the access charge neutral in a bypass decision.

Do you have any disagreement with that line of reasoning?

Mr. WOODY. The only thing I can say is I am not familiar with what the administration's policy is on the access fee, since it is so recently issued. I was in a plane when the decision came down.

Representative SWIFT. I understand that. I don't mean to put you on a spot, but I think we need to understand that that bypass fee—particularly the public agencies that may want to do it—that bypass fee is a tradeoff.

You eliminate the $8 a month in lieu of this, and municipalities and State governments that have reason to bypass can do so, and even if they pay that fee, if the tradeoff is eliminating that $8 a month for every telephone line that State or that city or that municipality, your consumers are well to the good.

Mr. WOODY. I guess my comment would be to reiterate that my purpose is to make sure that you are aware in this entire legislative process that there is an impact on the taxpayer by imposition of such a fee, and I would imagine that typically State government is the largest user in every State, and that you would see this same type of phenomenon across the entire country.

I would hope you would go to the different State governments and find out what the particular impacts would be. I am the only State here out of 50—where are the rest?

Representative SWIFT. We had someone representing the Governors' Conference yesterday. It is very appropriate that you bring it to our attention, but it might be very interesting if you were to work out the mathematics of it if we don't come up with some solution to bypass so that we can have an access charge from long-distance companies, and failing to do that, all your consumers get hit eventually with an $8-a-month fee, what economic damage you have done to the citizens under that as opposed to what costs they might have as taxpayers going the other way.

Mr. WOODY. I believe that the State utilities commission may have those figures.

Representative SWIFT. They might, and we will pursue that. One last question:

Mr. Kimmelman, I am not sure I understand what you mean by politically insulated, you need the cooperation of the telephone industry to get it politically insulated.

Mr. KIMMELMAN. I am not sure what it would take. My point is basically in comparison to other means-tested programs, or anything like even the windfall profits tax, where money was to be collected and distributed to low-income individuals that had need.

If anything is to be targeted at all, it must not repeat what has happened with the low-income energy assistance.

Representative SWIFT. Now, I understand that. I think that is a legitimate concern. Let me postulate, in return, because a number of you raised this point, I think it is a trap to buy any kind of a welfare approach to this rather than work very hard to preserve the present system.

What is so valuable about the present system of union service is you don't justify it on the basis you have got to help the poor, you justify it on the basis that you and I who can afford to pay those higher fees, pay a subsidy that flows to some of those low-income people, but we benefit because our telephone service is more valuable, and you don't have to worry about means-testing, about whether Congress will pass the appropriations, and you don't have to worry about people that are coming along and trying to restrict and tighten down and get rid of the cheats and the mess you get into, that you get into with welfare.

You simply continue a system that serves us well, and I urge you not to fall into that trap. I thank the chairman.

Mr. KIMMELMAN. Our concerns are the same. The only problem that we have with that line of reasoning is a concern that local rates are going up dramatically and to lop off the $2 access charge, which will be more down the road, and possibly an intra-State access charge may still leave many low-income people with overpriced telephone service they cannot afford.

Our concern is that we must go beyond that and make sure that they qualify for something else.

Representative SWIFT. Thank you.

Chairman **Dingell**. The Chair thanks the gentleman.

The Chair now recognizes the gentleman from Texas, Mr. Leland.

Representative **Leland**. Thank you, Mr. Chairman.

I would like to address my questions to Miss Ostrander. I have heard a lot about senior citizens. When I was in the Texas Legislature, I fought for generic substitution, and we got it a couple of years ago.

I realize the plight of senior citizens. I have piggy-backed on this issue with my colleague, Mr. Wyden. I am particularly concerned about the impact that these higher rates asked for in my region in particular, $1.7 billion increase to Southwestern Bell, how that is going to add stress to the senior citizens.

Just tell me, you have heard all the testimony that has been put forward by, earlier, the AT&T people and I am sure you heard the other folks who have argued for some kind of adjustments, because divestiture is causing all kinds of problems.

Tell me in your own words how this is really going to place a strain on our senior citizens, and if in fact you have any real solutions, what do you propose?

Mrs. **Ostrander**. I would hope that the two committees would bear in mind what we have said in our written statement. We would like to work with the committees in improving language and to help determine what is a viable lifeline, what are we really talking about?

One of the impacts which I did not go into, it is in part of my written statement, is that we have to look at what is happening with the senior groups, the 75 and above, the frail elderly, who need the telephone the most, many times it is not a question of even them being able to afford, it is a question of having it when they need it, of serving as reassurances for each other.

Some of them, when they start counting calls or whatever, start having difficulty with it. So, if they have a perception that that telephone bill is going to be beyond what they can afford, they simply will not do some of the basics like calling the doctor or ordering their drugs.

Some of those that are borderline at being able to be independent at home will soon well find, may—well, just catapult them into institutions.

That is a danger, a threat that is always there. But one of the areas that none of us have addressed has to do with what is also the impact of the telephone problems that are arising on the providers of service to the elderly, and that is an area that we don't want to close off.

It has to be open both ways. There is too much at stake both in terms of the quality of life for the elderly, but also as to what kind of expense are we imposing on the taxpayer as a result of poor decisions that are made now.

Representative **Leland**. I hear you saying something that has been bothering me for years, since I have been very sensitive to and aware of the problems of senior citizens, that when in fact the senior citizen could not afford the service or goods, they would just go without.

Mrs. **Ostrander**. And deteriorate faster.

Representative **Leland**. They are probably more fragile than everybody else and would rather suffer mentally and physically than seek——

Mrs. **Ostrander**. It is compounding. As we see the higher age group growing faster than any other segment, that group has probably several health problems and there you have additional problems by isolating them still further from their own community.

Representative **Leland**. Thank you.

Mr. Booe, let me ask you, what is the impact of divestiture on unemployment, if I might ask, or is there an impact?

Mr. **Booe**. It is hard to tell the overall impact on employment. Theoretically, there will be more jobs. The impact on the jobs of those we represent has been a depressing one, that there have been cutbacks, layoffs, there is a lot of uneasiness not knowing how to adjust to everything.

There has been a lot of movement of people. The biggest impact has been a cyclical one, I think, on the people we represent because for the history of this country, the telecommunications industry, if you worked for the telephone company, it was a kind of a career arrangement.

If you came to work and were hired and you spent your 40 years, kept your nose clean, you retired and you worked through the business. As a result, it attracted a certain group of people who were very security conscious, and now they are not sure that that employment security is going to be there.

Nobody knows for sure whether they are going to right now—they are still wondering whether they are going to end up in American Bell, or in the operating company, or end up in one of the other subsidiaries that are about to be set up, and then the concern about their pension portability and what the wage rates are going to be, hitting a group of people who never had to worry about those things before.

Representative **Leland**. It has been my experience that CWA has been pretty much empathetic with the problems of the consumers and have worked pretty much to that end. You have heard the problems for the senior citizens, minorities, other low-income groups of people and many times CWA people fall in that category.

What do you think about the promises put forward by those who would be your bosses or those who have been your bosses about solutions to the problems that divestiture has caused?

Mr. **Booe**. In addition to being employees in the industry, they are consumers, too. I believe we are directly related with the minority community and the rest of the consumers, including the elderly, and the policy decisions that our executive board is dealing with right now deal more from the standpoint of us as consumers than dealing with the issues of fair rate structures, that rates be fair to everyone concerned, most particularly to the consumers, but to the industry, also.

The suggestions that they have made to us recently have been across the bargaining table, and they are not satisfactory at all in dealing with the problems as we see them of divestiture and deregulation.

Representative **Leland**. I look forward to working more closely with you. I am really concerned about what we are seeing, and want very much to resolve the problem at least to some compromise position where our senior citizens in particular and our low-income people would not be hurt.

Thank you.

Chairman DINGELL. The Chair thanks the gentleman.

The Chair would like to commend our panel. We appreciate your concern for the problem of continuing our universal telephone service and for the importance of seeing to it that rates are fair for those least able to pay the costs of telephone service.

Mr. Booe, I want to pay a particular compliment to you. Your statement is one of the best I have read on this matter, and the break between your union and AT&T is, I believe, an historic event.

You say you see a flaw in the claim that the access charge decision discourages bypass. I believe what you are telling us there is that bypass can occur at almost any point in the system.

The minute you get an aberration induced by high costs which can be avoided by a user, bypass is going to occur.

Mr. BOOE. Any time there is an aberration, it may be cost or some other kind of basis that encourages bypass. The technology is there to bypass at almost any level.

Chairman DINGELL. I think your thesis is that bypass would be encouraged under the FCC's plan. Rather than at the point where the local system enters the interstate system, bypass would be encouraged at the very point where a user could enter the local net, isn't that right?

Mr. BOOE. Yes.

Chairman DINGELL. Would you want to elaborate on that?

Mr. BOOE. No, I think you have hit it. Where the user would enter the local net is another one of the places. The bypass could be encouraged by the access charge at any level.

Chairman DINGELL. And your thesis is that the FCC's action has simply moved the bypass potential back to the point where the individual picks up the telephone?

Mr. BOOE. Basically, I think our thesis is that the FCC thinks it dealt with something, and all it did was to move something around, just move it back.

Chairman DINGELL. The only way you can discourage that is by some kind of economic mechanism such as bypass charges, evenly and fairly prescribed in a fashion that would equalize charges at every point throughout the system for all users, isn't that right?

Mr. BOOE. Yes. Maybe the term discourage bypass is misunderstood. What we want to do is to make sure that a decision is made that if bypass is the right thing for that bypasser, not necessarily to discourage it, but to make sure that the bypasser pays a fair share of maintaining the public network that is there, because the bypasser will come back to the network and complain if the network is not there to take care of things.

Chairman DINGELL. Mr. Simon, your comment on the arbitrary nature of any means test for lifeline rates reflects a concern that I share. I would appreciate it if you would take time to address that question for us.

Isn't it the case that lifeline rates are workable only if basic monthly rates are low, so that the gap between basic and lifeline rates is small?

Mr. SIMON. I agree.

Chairman DINGELL. Doesn't this mean that lifeline rates can only be a safety net and that the primary emphasis must be placed upon measures that maintain the affordability of basic rates for all?

Mr. SIMON. Yes. In fact, in my written testimony, I suggest that lifeline ought to be a function of rate structure, although I want to make clear I am not suggesting local measured service. There are lifeline-type rate structures that would be available to everybody whom they suited without regard to income or other personal data.

Chairman DINGELL. Would you want to comment on the applicability of a means test to the problems of the postdivestiture period with regard to the telephone rate structure of this country?

What will be the situation there if we address it solely by creating some kind of a means test lifeline rate?

Mr. KIMMELMAN. I certainly don't believe that will be enough. If we are going to have dramatic rate increases, we need to do something about the access charge. Even if the access charge is eliminated, there still will be dramatic upward pressure on local rates, so I think there will still be more need for some sort of a lifeline.

The point about the means testing, we don't inherently like it. Theoretically, it sounds good, but we know that politically it is extremely difficult. We are concerned that enough money be provided to subsidize the very poor to be sure they can get a telephone.

If we just lop off a few dollars on everyone's bill, we are not convinced that the very poor will be protected.

Chairman DINGELL. It is also true, however, that if you don't deal with the bypass problem, which shifts the costs further into the local service net, a lifeline system will oppress those who are just above the level at which the means test permits them to enter the system, isn't that true?

Mr. KIMMELMAN. Yes. Our concern is that if there is anything that resembles a means test, it not be a very narrow one, that it be one that goes beyond the Federal entitlement programs that currently exist.

Chairman DINGELL. The problem with your means test or the problem with your lifeline is that those who achieve the benefit of lifeline get it at the expense of other users, and they might get it at the expense of users who are only marginally better off than lifeline customers and who might be persons of very, very limited means.

Mr. KIMMELMAN. Yes. That is why we support the concept of some pooling of revenue, particularly from either equipment charges or interstate usage charges, the money must come from somewhere outside the local network to help States that have a peculiarly high number of poor, elderly, unemployed, or handicapped people.

Chairman DINGELL. What do you think about the means test again?

Mr. KIMMELMAN. We are concerned. Our argument is that if the industry would cooperate and help structure something that they themselves could administer; and that would not be embarrassing for someone to apply for the targetting could work. Or if Congress just mandates a lifeline rate it is possible that there would not be much oversubscription. So long as lifeline would cover all the poor, that is all we need.

My concern is that it is not something that would be a political problem down the road where Congress claims it is taking care of the poverty problem, but it does not really do it.

Chairman DINGELL. Thank you very much.

The Chair is going to recognize Mr. Wyden.

Representative WYDEN. I thank the Chairman.

There aren't all that many causes that I would risk having a coronary for, but I sprinted back and forth just to ask you a couple of questions, Mrs. Ostrander, to focus on the particular concerns of senior citizens.

I think the whole history of means tests as far as senior citizens has been a disaster. I was director of the Gray Panthers for several years before I came to Congress, and with every program that we faced, we had the difficulty of getting help to the seniors that needed it most.

The reason is on occasion after occasion, we ran up against one word, which was welfare. The first thing out of their mouths was, is that another welfare program? My concern is, and I have heard it from my senior citizens now, because I have had several meetings on telephone rates in Oregon, is that they think we are heading down that same path right now, instead of trying to come up with a system that particularly looks to insure universal service for people of modest means, instead, we are trying to come up with a special welfare system or means test just for the elderly.

My first point is let's work together, so we don't become part of that history of means tests, because with respect to senior citizens, it is clear, they see that welfare stigma and they refuse to be a part of such a system.

The first question I have for you dealt with exactly what the effect would be of these rate increases? Now, I see millions of seniors on the economic tightrope. They balance their food against their fuel and their fuel against their medical care.

Any increase right now will push some of those seniors off the tightrope. We have some phone company executives, not all of them, but some came and told us that come January, it is not going to be any big deal, you will just get another bill and you will be able to pay it.

What is your feeling as to what is going to happen in January with respect to senior citizens as of the situation as it stands today?

Mrs. OSTRANDER. I think we have all heard about the amount of rate increases that local companies are asking for. I testified at our own local company rate hearings last week. There is some real serious concern that at that local level where they are the ones that are really going to be affected immediately, they have a feeling that the one thing that they needed and wanted and depended on is suddenly going to force them into some additional decisions.

I think you hit on some of the things that are bothering the seniors. What is in my statement, and I did not elaborate on, is the fact that within the last several years the rate of poverty among the elderly is increasing, but also there is that 10 percent gap between those at the poverty level and those within 125 percent of poverty level that are hurting very bad.

We have health care costs right now that are climbing extremely fast. We have utility bills that are climbing extremely fast, even with energy assistance. It does not do the total job.

What we are asking again, over and over and over again, is in the basic necessities as they climb, that the elderly must make tough decisions.

Representative WYDEN. I will take that as an answer that you see evidence right now of these phone bills causing some real hardships for some of the seniors, is that correct?

Mrs. OSTRANDER. Yes, and this is very well—our committees, our State legislative committees across the country are all asking our staff for guidance in terms of how to deal with the local rate requests that are coming through.

Representative WYDEN. The only other question that I had dealt with measured service. I have some very fundamental reservations about measured service. I think we all understand that the telephone is a lifeline for seniors, they may have nothing except it and the chance to call a doctor to take care of emergencies and necessities.

Do you think there is any way that a measured service phone approach could work for senior citizens, and if so, tell us how?

Mrs. OSTRANDER. No. As a matter of fact, I testified before a subcommittee of the House Select Committee on Aging recently on that issue.

There are many reasons why that is the most difficult one for them to accept. They use it as a social instrument, and whether you go to local measured service, that knocks out the social instrument.

If they call, say the social security office or the doctor's office and they are put on hold, they are going to panic. They can't deal with it. So there is in my estimation, no viable way to work it out.

Our organization has sat and evaluated that extensively, and it is the one area that gives us the most problem.

Representative WYDEN. You can probably answer this with just a yes or no. My feeling, as I read your testimony, you essentially wanted us to flush out the lifeline kind of approach.

Mrs. OSTRANDER. Yes, I think we need to look at all the differences and come up with something that will not vary so much from State to State, something that the elderly can begin to identify with and hang on to as what they know, they will get to know as at least the basic.

Representative WYDEN. The reason you want us to flush out that lifeline approach is because you fear if we don't do that, there could be measured phone systems around the country?

Mrs. OSTRANDER. Yes.

Representative WYDEN. Thank you, Mr. Chairman.

Chairman DINGELL. The Chair thanks the gentleman.

The Chair wants to express our appreciation to the panel. The Chair observes that getting this legislation enacted into law is going to be thoroughly possible, but also thoroughly difficult.

We hope that we will have your assistance in our undertaking.

Ladies and gentlemen, we thank you. The committees stands adjourned until the call of the Chair.

[Whereupon, at 2:25 p.m., the hearings were adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

STATEMENT OF HON. THAD COCHRAN, U.S. SENATOR FROM MISSISSIPPI

Mr. Chairman, I welcome the opportunity to express my views about legislation to preserve universal basic telephone service at affordable rates.

I commend you on your efforts to address this pressing issue in such a timely and effective manner. Joint hearings help to ensure prompt Congressional action.

I am pleased to be a cosponsor of S. 1660. The availability of universal basic telephone service is a concern many of us share.

Recent requests for rate increases in telephone service all over the country have instilled in us grave concerns that local telephone rates could skyrocket to alarming and unreasonable levels as a result of the AT&T reorganization, and the actions of the Federal Communications Commission.

The theory of universal basic service is not new. Indeed, it is the backbone of the Communications Act of 1934 and all subsequent telecommunications legislation. Our legislation reiterates the desire of Congress to ensure the continuation of such service by providing a system of access charges that will distribute the cost of telephone service is such a manner as to preserve the affordability of telephone service for consumers.

What this legislation is designed to protect against is a shift in much of the cost of maintaining the universal telephone network from the major users of the network to the residential telephone customers. Such policies would surely result in the destruction of universal service.

If such a cost shift were allowed to occur, it would most directly and dramatically affect rural and low-income subscribers. In my home state of Mississippi, we have an abundance of both these subscribers. The divestiture of AT&T, further regulatory changes by the FCC, and the rapid emergence of new telecommunications technology require that Congress institute a permanent, reliable protection mechanism to prevent rural and low-income users from suffering from the brunt of what should be viewed as progress in the industry.

In my view, S. 1660 affords Congress such a mechanism. The role of Congress is in the oversight of the FCC's access charge decision. The practical effect of this decision is to raise the up-front charges which local subscribers must pay to obtain phone service. I think the subsidy mechanism in S. 1660 more usefully and necessarily targets its protection to rural and low-income users, where the greater need exists.

Many other important issues must be and are addressed by S. 1660, but they all speak to the end result of ensuring universal basic telephone service at affordable rates. I know as these Committees meet and refine the proposals before them, we can come up with a bill that satisfies the concerns of the industry, the states, the FCC and the consumers.

STATEMENT OF HON. THOMAS DASCHLE, U.S. REPRESENTATIVE FROM SOUTH DAKOTA

Mr. Chairman and Members of the Subcommittee I appreciate this opportunity to testify today on recent developments affecting the U.S. telephone industry and the need for legislation to insure the maintenance of affordable and universally available telephone service for all citizens. As you are aware, we are witnessing some of the most dramatic and far-reaching changes in the telephone industry since the invention of the telephone by Alexander Graham Bell decades ago. Without question, the AT&T divestiture will result in profound changes in the telephone industry that we have all come to take for granted. Though I believe that in the long term the divestiture will result in more choices of equipment and service, it will in the short term cause upheaval. The impact of divestiture itself is still somewhat uncertain, especially on the local telephone companies which will now operate independently of AT&T. I am concerned that many of the rate increase requests by these local telephone companies before state public utility commissions may be somewhat premature. In South Dakota, a $21.5 million increase was requested, though only $7.5

million of the request is to mitigate the impact of divestiture and the loss of long distance subsidies. This is in direct conflict with testimony of AT&T Chairman, Charles Brown, who last year stated that divestiture would not result in increased costs. Unfortunately, the terms of divestiture are now set and state utility commissions will henceforth have primary responsibility for determining whether these rate increases are justified or not.

Where Congress can play a significant role is in addressing the FCC access charge decision, which transfers billions of dollars of network costs from long distance telephone companies to local telephone customers. The FCC access rate decision was completely contrary to what the divestiture agreement had envisioned and will result in additional costs of at least $8 a month by the end of the decade. This user fee would be paid by local customers for access to long distance telephone lines whether they called long distance or not. Inevitably, the elderly and poor would have to forego telephone service which would further increase costs for those still desiring service. In my view, the access charge decision should be delayed indefinitely or amended to require continued long distance payments to local telephone companies for use of local services. Any exemption for the long distance carriers still using local services would be an unwarranted windfall.

Regardless of how the access charge decision is resolved, an important and necessary safeguard would be the establishment of a Universal Service Fund (USF). This would insure that telecommunications services which currently allow large-volume customers to bypass local facilities are required to contribute to maintenance of local systems and services. Those areas, many of which would be in rural states like South Dakota, would then be reimbursed for costs above the national average. Ideally, a formula requiring total reimbursement of all costs above 110% of the national average, as advocated by the National Rural Telephone Coalition (NRTC) should be adopted.

Finally, I believe we have a moral responsibility to provide "lifeline service" to those who may be burdened beyond their ability to pay for continued service as a result of the changes in the telephone industry. Legislation should provide for minimum local telephone services at reduced rates for low-income and elderly persons who might not otherwise be able to afford continued telephone service.

Though I have not come here today to endorse any particular legislation, I believe it absolutely imperative that Congress take action to limit the impact of the FCC access charge decision which it has been estimated will cost consumers $1 billion a year. There is little justification for placing the entire burden of local costs on local users when long distance carriers also utilize these local services. As stated, an appropriate safeguard for continued service in high cost areas would be the establishment of a Universal Service Fund to reimburse local companies for above average costs. Only with legislation restricting or eliminating the FCC access charge decision and the addition of a Universal Service Fund and lifeline rates will we insure that basic telephone service at affordable cost will continue to be a national priority.

Statement of Hon. Edward I. Koch, Mayor, City of New York

The telecommunications industry is at a watershed. As a direct result of the national movement towards more telecommunications competition, the subsidy of local service by long distance service will be eliminated. The FCC has mandated that local telephone companies levy a substantial access charge for every line used by local telephone subscribers. This charge—which will apply to the cost of linking a local subscriber to the long distance network—is designed to pay a local cost that heretofore has been subsidized by long distance.[1]

Logically, therefore, long distance rates will drop and consumers—big and small alike—will pay less. For the City of New York, however, access charges will cost an additional $4.78 million, the salaries of 140 police officers.[2] The City is not a particularly active long distance dialer (it represents only 5% of our annual bill), nevertheless we will have to pay access charges near equal to its entire long distance bill in the first year [3], rising to $7 million in the second. These charges, incidentally, are totally unrelated to usage.

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[1] These access charges are $2 per line per month for residential customers (increasing to $4 monthly in 1986 and $6 in 1989), and $6 per line per month for business users (which will remain at $6 monthly through 1986, and which may rise thereafter).

[1] For 150,000 City lines

[2] From $6.1 million in FY to an estimated $10.88 million

At the same time, experts tell us, we can expect our local dialing costs to rise dramatically since they will no longer be subsidized. Some experts expect local rates to double. As a corporate user, therefore, the City can expect to see these costs go from $20 million to $40 million annually. That's another 600 police officers.

These extra costs will be compounded by intrastate access charges which are part of rate increases pending in many states. These local rate increases total $7.5 billion nationwide.

If New City as a rather large corporate user [4] is having trouble accepting these increases, individual New Yorkers and thousands of businesses—large and small—in the five boroughs will, too.

Therefore, I share the concern of many members of Congress about the threat the FCC decision poses to Universal Service for the poor and needy members of our society. Since the 1934 Communications Act, which called for "universal service at a reasonable rate," we have been moving towards that ideal for all Americans.

But for large numbers of poor and lower income New Yorkers, the $2 monthly access charge will be a burden—for a service that they may not even use. This increase threatens the concept of universal telephone service. This ideal must be maintained—our telephone system is only as good as the number of people it serves.

As numerous studies have shown, increased utility rates have a far greater impact on low income households than higher income households. One such study showed that for households with incomes in the bottom ten percent of income distribution, the fraction of income devoted to utility payments was 15 percent, or six times that expended by households in the top ten percent [5]. As a result, the $2 monthly access charge will place a disproportionately greater burden on the poor and those on fixed incomes. This may cause them to forego home telephone service, thereby threatening the very concept of universal service.

It is true that the FCC decision makes provision for a "lifeline service" for the poor and needy, subsidized according to their need. But the implementation of this mandated lifeline service is insufficiently defined and too vague to be relied upon by the poor, the needy, and those who are fighting to protect them.

The FCC's decision—the details and impact of which are still vague—can be overruled by Congressional legislation.

The thrust and purpose of legislation pending in the House and Senate are identical, and they are almost identical in their means of achieving that purpose: repealng the access charge, and establishing an alternative method of apportioning the costs of reconfiguring the national network in order to facilitate competition.

One alternative method is the so-called Universal Service Fund, a well-intentioned palliative to lessen the impact of soaring local telephone costs. However, no one guarantees that this Fund will mean lower costs to consumers. Its implementation is unclear.

Nor is it clear that these bills will provide incentives to inefficient phone companies to improve service, and, indeed, efficient phone companies may even have major incentives to let service slip. These possibilities simply have not been explored. Many experts assert that such a fund would create major regional differences, favoring newer, growing systems over established systems, inefficient systems over efficient systems. We want to ensure local rates don't create a new class of communications poor, but we also don't want New Yorkers to subsidize less efficient systems elsewhere.

Another alternative is a share on so-called bypass operations, which by definition do not, and will not, use any common local or national telecommunications network. Such a charge seemingly apportions costs to those who have benefitted from decades of technological innovation, those who are seemingly best able to pay. However, will such a chart stifle new technological innovation? Do we want to intervene where new technology is being utilized to provide efficient, cost-effective service? Would such a charge have a deleterious impact on a major project like Teleport on Staten Island?

The complexity and far-reaching potential of what you do here is clear: you may forever alter America's successful experiment with "universal service at reasonable cost."

There are several critical needs: to protect the ideal of universal service especially for the poor and needy; to achieve a more realistic cost-basing pricing for telephone service; to encourage competition, efficiency and technological innovation; and to ensure the maintenance of the most advanced, most accessible telecommunications system in the world. I am not sure that these needs are being met under any of the present proposals.

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[4] FY costs: $98.7 million (est.)

[5] Hill, "The Impact of Natural Gas Deregulation on American Families," Economic Outlook U.S.A. pp. 84-87, 85 (Autumn 1981).

It seems that all present proposals merely treat symptoms and not the underlying causes of premium rates for local telephone service. The key to meeting of the critical needs is a revised local rate structure. But what comprises local rates has been, heretofore, extraordinarily vague.

We must determine exactly the components of local rate increases, identify potential economies and determine where subsidies are legitimately required. In this way all subscribers will know that any extra charge each month is helping pay for basic telephone service for an elderly couple down the block, not for telephones in the vacation homa of an executive.

Whether this investigation of local rates should be undertaken at the Federal or state level, or both, is a matter still open for discussion. Until we've identified the root of the problem threatening universal telephone service—spiralling local rates—we should be extremely cautious about the way we structure our solutions. The American public can afford to use it. We don't want that to change.

There is no "painless" solution. A price restructuring is inevitable, and dislocations will occur. But we must minimize them through a deliberate and methodical analytic process.

Thank you.

STATEMENT BY NIELSEN COCHRAN, CITY COMMISSIONER OF JACKSON, MISS.

Mr. Chairman, my name is Nielsen Cochran, City Commissioner of Jackson, Mississippi. I appreciate the opporunity to submit my written testimony regarding your Committee's hearings on future local telephone rate increases. This is a problem which needs immediate attention, and I commend you and your Committee for taking this step in order to address this issue.

As a municipal elected official since 1977, it is my responsibility to see that basic services are delivered to our citizens, while at the same time generate an atomosphere for economic and industrial growth. This must be accomplised with an understanding of the limited financial resources of our citizens here in Mississippi.

I am gravely concerned aobut recent reports that our local telephone rates "could double in 1984 and possibly triple by 1985" because of certain decisions made by the FCC and our Federal Courts. Mr. Chairman, our local consumers simply cannot afford this type of possible rate increase. A lot of our citizens will have to have their phones removed or either do without essential life-support services if this is allowed to take place.

Congress needs to take immediate action to generate an appropriate vehicle by which revenues can be generated in order to offset proposed higher local telephone rates. Our residential and rural communities will be faced with a devastating disruption in communications if this universal problem is not resolved.

A National policy at the Congressional level must be established in order for State Public Utility Boards or Commissions to properly address proposed future local telephone rate requests. This policy should insure the availability of access to minimum basic telephone services to all of our citizens at a reasonable rate. I further recommend that a National Board be establihsed in order to continue to monitor the ever-changing technology as it relates to the telephone industry in order to insure proper implementation of any legislation which is adopted to insure that universal telephone service is provided at a reasonable rate.

This is a very confusing period for the telecommunications industry while AT&T is being reorganized. Our consumers must be assured that during and after this transition takes place that they can continue to receive this life-support service at a reasonable rate. We must be sensitive to the financial concerns of our consumers.

STATEMENT OF THE AMERICAN PETROLEUM INSTITUTE

The American Petroleum Institute (API) is pleased to have this opportunity to present to the Senate Committee on Commerce, Science and Transportation and the House Committee on Energy and Commerce its views on S. 1660 and H.R. 3621, the Universal Telephone Service Preservation Act of 1983.

PRELIMINARY STATEMENT

API is a national trade association representing approximately 275 companies and 6000 individual members. API's membership is representative of all sections of the petroleum industry which are engaged in the exploration, production, refining, marketing, and transportation of petroleum and petroleum products. Among its many activities, API acts on behalf of its members as a spokesman before federal and state agencies and legislative bodies. API's primary committee is concerned with telecommunications matters is its Central Committee on Telecommunications which is supported and sustained by more than 700 petroleum and natural gas company telecommunications users.

Our comments address primarily those sections of the legislation which would have a significant adverse impact on privately owned and operated telecommunications systems of petroleum and natural gas companies. API believes that the legislation, as proposed, will erode the competitive nature of the telcommunications environment and discriminate against users of privately owned telecommunications systems.

By penalizing any entity that chooses to use such private facilities in lieu of exchange access facilities, the legislation will reduce technological innovation and impede competition by vesting exchange carriers with a legislatively protected monopoly over the provision of local exchange service. This, in turn, will remove incentives for exchange carriers to (1) provide high quality, reliable facilities, (2) offer prompt installation and repair services, and (3) make the necessary capital investments to meet future industry needs. These developments will perpetuate existing exchange network inefficiencies which are the foundational reasons privately owned facilities came into existence.

Clearly, these consequences would be contrary to the underlying goals of the AT&T divestiture and effectively discourage competitive pressures or incentives to provide efficient service and implement new technologies to meet our nation's rapidly expanding dependence on reliable telecommunications systems. Therefore, API believes that modification of certain provisions of S. 1660 and H.R. 3621 pertaining to access charges, universal service charges, and notification requirements is necessary.

ACCESS CHARGES

1. Why API Members Use Private Telecommunications Systems

The petroleum and natural gas industries rely heavily on a wide variety of telecommunications services and facilities in all phases of energy exploration, production, refining, transportation and distribution. These industries depend heavily on privately owned and operated land mobile systems, microwave systems, and wireline telephone systems. API members are also using satellite based systems and are currently examining the application of fiber optics systems. These systems are operated to improve productivity and to promote safety in meeting our nation's energy needs. They are not used to provide "for hire" or "for profit" telecommunications services to third parties. Rather, API members operate their own private systems to ensure complete control over the availability, on a timely basis, of quality communications transmissions. This control is important because telephone company facilities, especially the local exchange or "local loop" facilities, often cannot meet the unique telecommunications needs of API members; or, when such needs can be met, the service is frequently not available within the required time frame.

These privately owned telecommunications systems provide for the transmission of voice and data traffic, including facsimile, teletype, teleprocessing, telemetry, surpervisory control, data acquisition, and remote control. Such telecommunications systems are essential in order to serve diverse, and often remote, areas where the petroleum and natural gas industries must search for, produce, and transport essential energy products. The varied operating areas and conditions of the petroleum and natural gas industries create the need for the availability of nearly every basic form of telecommunications transmission service.

As previously mentioned, even in areas where exchange carrier circuits can be secured, these circuits cannot be relied upon, in many instances, to meet API members' multi-faceted telecommunications requirements. A telecommunications circuit serving critical telemetry, control, and data operations is no more reliable than its weakest link. Experience has shown that the local exchange portion or "local loop" of any telecommunications circuit is the portion most susceptible to failure and thus is the weakest link in the system. Reliable telecommunications services are essential to safe and efficient energy industry operations. The industry must have the flexibility to satisfy its telecommunications requirements.

Because API members have unique operational and reliability requirements they choose to use private telecommunications systems. Thus, the use of these private systems is not interchangeable with the use of local exchange facilities. Accordingly, API submits that H.R. 3621 should be modified so as not to discriminate against entities, such as API members, which use private systems instead of exchange access facilities. Specifically, Section 221(e)(3)(B)(iii) of Section 4(b) of H.R. 3621 should be amended to indicate that users of private systems shall not have to pay a charge reflecting the "availability" of exchange access facilities. There is no justification for imposing such access charges on private systems that do not interconnect with local exchange facilities, especially when such telephone facilities often cannot meet the needs of private system users.

In addition, API urges that Section 221(e)(4)(A) of Section 4(b) of H.R. 3621 be clarified so that this section applies solely to entities that bypass exchange carrier facilities in order to provide a "for-hire," competitive service and does not apply to private systems, such as those used by API members, that do not operate on a "for-hire" basis. These suggested revisions will ensure that users of private systems are not penalized for using necessarily more reliable communications systems to meet their operational requirements.

2. Access Charges Should be Cost-Based

Legislative guidelines for levying access charges should ensure that such charges are imposed on a cost-causative basis. Since access charges are designed to offset exchange carrier costs for providing exchange access, the charges should be cost-based. Accordingly, private system users should only pay access charges based on the number of lines actually interconnected to local exchange facilities.

In this regard, API endorses the principles set out in Section 221(e)(2)(B) of Section 4(b) of H.R. 3621 and believes that these principles should be incorporated into Section 221(e)(3)(A) of Section 4(b). The provisions of Section 221(e)(2)(B) require that exchange carrier access charges be justified by costs and prohibit imposing access charges for types or elements of exchange access that are not requested and obtained. Owners of private systems should to be required to pay the costs for exchange facilities that they do not use.

UNIVERSAL SERVICE CHARGES

Section 4 of S. 1660 and Section 5 of H.R. 3621 would amend the Communications Act of 1934 by providing subsidies to ensure the continued availability of universal telephone service at reasonable and affordable rates. API believes that certain universal service provisions should be modified in order to foster competition and promote cost-based pricing. For example, we are concerned that the literal language of proposed Section 410(e), as embodied in Section 6 of S. 1660, could be construed to proscribe or prohibit the use of any private telecommunications facilities. While the section requires "intent" to deprive an exchange company of access charge revenues, the provision could apply to any voluntary selection of private systems over local exchange facilities, thereby prohibiting the use of private systems altogether.

Although this section appears to be designed to penalize entities who fraudulently avoid paying access charges, its practical effect would be to penalize users of private systems in the areas previously described. This will deter the deployment of new and innovative technologies and deprive the energy industry of the freedom of choice in selecting the means of meeting its critical telecommunications requirements. Accordingly, the language should be modified so that use of private systems in lieu of exchange access facilities would be acceptable.

In addition, API believes that the universal service charges as proposed in Section 201(c)(1) of Section 4 of S. 1660 should be based solely on the number of lines that actually interconnect to local exchange facilities.

NOTIFICATION REQUIREMENT

The notification requirement in Section 221(e)(6)(A) of Section 4(b) of H.R. 3621 is unduly burdensome and should be eliminated. This provision requires virtually all owners of communications equipment who do not use the local exchange to notify the local exchange carrier, Federal Communications Commission, and appropriate State commissions. In addition to creating additional federal and state regulation, this requirement will impose a costly and unwarranted burden upon all affected entities. This reporting requirement could be eliminated by requiring an exchange access subscriber to pay access charges based solely on the number of lines that actually interconnect to local exchange facilities.

STATEMENT OF TOM KRAJEWSKI, VICE PRESIDENT OF AGRICULTURAL COOPERATIVES, GOVERNMENTAL AFFAIRS AT THE COOPERATIVE LEAGUE OF THE USA

Mr. Chairman, members of the committee. My name is Tom Krajewski. I am vice president of agricultural cooperatives, governmental affairs at the Cooperative League of the USA. I appreciate the opportunity to appear before you today to speak on behalf of the members of the Cooperative League, a trade association representing the American cooperative business community, and especially on behalf of our rural telephone cooperative members and the rural residents they serve. The Cooperative League supports all efforts in order to continue our universal telephone system presently in place.

Rural telephone cooperatives first came into existence as an answer to the growing need of rural residents to be able to communicate via telephone with other persons in nearby or distant areas and to be able to communicate as easily as urban dwellers.

The Bell System did not see an economic benefit to providing rural areas with telephone service which forced the rural area residents to form their member-owned telephone cooperatives in order to have access to affordable telephone service and its economic and social benefits.

Over the years America's telephone system has grown and developed into the best system in the world. The AT&T divestiture and the advent of specialized long-distanced telephone service companies serving high-volume users has brought into question continued access to high-quality telephone service by all of America.

The ability to bypass long-distance system specialized telephone companies reduces the traffic on regular long-distance facilities thereby increasing the per unit costs for normal long-distance service. This cost will be borne by those who are not high volume users causing them to discontinue their service. To deprive certain customers of access to telephone service, affordable telephone service is to jeopardize 50 years of work attaining nearly universal service.

Since the AT&T divestiture, the FCC has designed an access charge mechanism where all subscribers will be charged a monthly flat rate in order to be able to make interstate calls. In addition to the flat rate charge there will be usage charges with the greater burden of these costs falling on customers in the rural areas as the telephone companies serving these areas incur higher unit costs in comparison to most other telephone companies.

The FCC has also added the universal service fund as a means to help these higher per unit cost companies keep access charges at a reasonable level. Gathered from funds collected from all long-distance users, it will have a positive effect on the availability for all customers of a universal phone system.

The value of a telephone is not in the answering of a call from Sears, but in the calling of my Uncle Joe in Babbit, Minnesota. The value to Sears of course is to be able to call both of us. Everyone benefits from universal service—everyone should pay for it. Sears and other major and minor businesses may find it economical to bypass the main system but without adequate support They may find far fewer customers at the other end of the line.

The Cooperative League supports the idea that bypassers of local telephone facilities should be made to contribute to the upkeep of our current universal system through the universal service fund.

The technology of 1983 requires legislation to continue Congress's original mandate assuring the continuation of America's universal telephone system and availability of access to it at an equitable rate.

The Cooperative League on behalf of its members supports the original intent of Congress to ensure that citizens in all areas of the United States continue to have access to affordable telephone service and to ensure that we continue to have access to each other through the telephone.

Thank you.

STATEMENT OF THE UTILITIES TELECOMMUNICATIONS COUNCIL

The Utilities Telecommunication Council (UTC) is pleased to have this opportunity to present the Senate Committee on Commerce, Science and Transportation and the House Committee on Energy and Commerce with its views on S. 1660 and H.R. 3621, the Universal Telephone Service Preservation Act of 1983 (the Act).

I. PRELIMINARY STATEMENT

UTC is the national representative on telecommunications matters of the nation's electric, gas, water, and steam utilities ("Energy Utilities"). More than 2,000 of these Energy Utilities are members of UTC. They range in size from large investor-owned or municipally-owned urban utilities providing gas, electric, water, and steam services to several millions of consumers to small rural electric cooperatives and small water districts serving only a few thousand customers.

II. SUMMARY OF CONCERN

UTC is concerned that the proposed legislation will stifle competition and foster a monopoly of the local exchange at a time when competition should be encouraged. UTC is also concerned that the legislation will have an adverse impact upon the privately owned and operated telecommunications systems of the nation's Energy Utilities and that this impact will, in turn, jeopardize the provision of vital utility services to the American public.

III. DISCUSSION

A. "Bypass" or "Non-Use" Penalties Will Foster Monopoly in Local Exchange at a Time When Competition Should Be Promoted to Maintain Universal Telephone Service

Section 6(a) of the Senate bill would add a new subsection (e) to Section 410 of the Communications Act of 1934, which would essentially prohibit any bypass of the local exchange. Specifically, subsection (e) provides a fine of up to $100,000 for anyone bypassing the local exchange. Although it does require "intent" to deprive an exchange company of access charge revenues, the provision could be interpreted to include anyone who chooses not to access the local exchange.

Similarly, under the access charge scheme proposed in the House bill, anyone who indirectly interconnects to or bypasses local exchange facilities will have to pay a "nonuse" or "bypass" penalty reflecting the availability of local telephone facilities as an alternative. See proposed §§ 221(e)(3)(B)(iii) and 221(e)(4)(A).

UTC assumes these penalties were included because the Committees believed they were necessary to ensure universal telephone service. This is, however, a misconception. The penalties foster the existing monopoly in local exchange services by discouraging all alternative means of local exchange and access service, including the use of private telecommunications systems even though these private telecommunications systems are needed to provide a degree of reliability and, in some cases, capacity not found in the local loop. These bills also attempt to ensure universal service by keeping local telephone rates at a low level through "access charge" payments from long-distance telephone carriers (and thus, their customers) and operators of private systems.

An alternative way to maintain low local exchange telephone rates and thus maintain, if not improve, universal service is to encourage competition in local exchange services similar to what has already been done in the areas of Customer Premises Equipment (CPE) and interexchange telephone service. If the $10 telephone and plummeting prices for interexchange telecommunications service are the result of competition, competition should also bring about a similar effect in the local exchange market. Insofar as universal service is concerned, it would be in the self-interest of all the competitors in the market to work out arrangements whereby customers employing different systems could inter-communicate with each other. If the market does not accomplish this, it could be brought about by appropriate regulation. However, UTC believes that the market influence would be so strong as to obviate the necessity of any government intervention to maintain universality, as, again, it would be in the best interest of all competitors in a market to ensure that their customers can communicate with all other customers in that market.

Therefore, rather than placing restraints on systems which could be competitive with the existing local exchange companies (i.e., cable systems, new fiber optic system competitors, and cellular radio systems), UTC suggests that it would be in our nation's best interest for Congress to encourage competition in the local exchange market, as has already been done in the interexchange and CPE markets.

Judge Harold Greene in his opinion in *United States* v. *Western Electric et al.*, (Ci. Ac. 82-0192) filed April 20, 1983 stated, at p. 32, that with respect to intra-LATA competition to local exchange carriers from interexchange carriers:

"[T]he lack of competition in this market [intra-LATA] would constitute an intolerable development. The opening up of competition lies at the heart of this lawsuit and of the decree entered at its conclusion and the significant amount of traffic that is both intrastate and intra-LATA should not reserved through the monopoly carrier."

Thus, UTC urges that these bills be purged of those provisions which place restraints on systems, private or otherwise, which are dubbed "bypass" systems. Furthermore, any legislation adopted should encourage the injection of competitive forces into the local exchange market.

UTC suggests that fair and reasonable access charges, based on actual usage of the local exchange service by those inter-LATA or interexchange carriers who interconnect to the local exchange system, would provide the necessary "cushion" during the transition from a fully regulated to a fully competitive local exchange market. Maintaining an absolute, ironclad monopoly on local exchange service would deter technology as well as reduce the reliability of essential communications, such as those needed by the Energy Utilities, and flies in the face of over 25 years of evolution in the American telecommunciations market, specifically the Modified Final Judgment as approved by the Court.

Continued monopoly in the local loop would contravene the primary purpose of the Act—to promote universal telephone service—by driving local telephone rates upward. It would hardly "encourag[e] continuing improvements in telecommunications techologies and service . . ." [1] or "establish incentives for efficient investment decisions and technological choices. . . ." [2]

For the reasons discussed above, competition, not monopoly, should be fostered with regard to local exchange. Accordingly, the "bypass" and "nonuse" penalties should be removed from the Act. If, however, the Committees are not persuaded by the arguments supra, UTC submits that the private not-for-hire systems oeprated by Energy Utilities should be excluded from the penalties.

UTC opposes assessment of a "bypass" or "non-use" penalty against Energy Utilities operating private not-for-hire systems which are either indirectly interconnected or not interconnected at all with the local exchange because such penalties would threaten the Energy Utilities' ability to provide vital utility services to the American public. The "bypass" or "non-use" penalties are based on a fundamental misconception regarding the reasons for which private systems are used. The Act assumes that the use of private systems is interchangeable with the use of local exchange services, and that one can be substituted for the other. Therefore, it erroneously assumes that operators of private systems would bypass the local exchange or choose not to subscribe to local exchange facilities for the sole purpose of avoiding charges imposed by the local telephone companies. However, Energy Utilities operate private systems because they need redundant communications and systems under their control, and because they cannot obtain from the local telephone companies the quality or reliability of service which they require.

The Energy Utilities represented by UTC rely upon a wide variety of telecommunciations systems in all phases of their operations. The term "private telecommunciations system" refers to not-for-hire, user-provided telecommunications facilities which are used to support a user's primary business activity. The term includes user-owned and operated private land mobile radio systems, private operational-fixed microwave systems, electric utility power line carrier systems, user-owned wireline telephone systems and voice and data switching systems, user-owned satellite earth stations, user-owned fiber optics systems, to include any future transmission mediums. These systems are essential in order to service specialized industry needs and to provide communications which are under the user's control at all times.

Energy Utilities began installing their own private telecommunications systems because common carrier services were unavailable or could not adequately meet Energy Utilities' requirements. Specifically, common carriers have not been able to provide the high degree of reliability necessary for efficient provision of continuous utility services; nor have they been able to provide in many cases the types of services necessary to perform the functions required by the Energy Utilities. In order to carry out the task with which the Energy Utilities have been charged, namely that of providing utility services to the American public on a continuous basis 24-hours-a-day, seven days a week, Energy Utilities must have extremely reliable telecommunications which are always under their absolute control, particularly in emergency situations. This was highlighted in the Advisory Committee Report to the Federal Power Commission, entitled "Prevention of Power Failures," released in June of 1967, which directed that:

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[1] Sec. 2 of S. 1160.

[2] Sec. 3 of S. 1660, proposed § 221(e)(4).

"All critical communications facilities, particularly those having to do with relaying and control of important circuits and other system elements, *should be the responsibility of the operating utility and under its complete control.* [Emphasis added.] Volume II, p. 23.

While that Report dealt with communication for electric systems, the same basic considerations apply equally well to private communications systems of other gas and water utilities.

Without the ability to operate private systems, Energy Utilities would be without reliable communications systems under their complete control. Utility services to the American public would be subject to serious disruptions (such as occurred in the 1965 Northeast Blackout). Very few segments of the public, industry or government, including the defense establishment, can effectively function without vital Energy Utility services. Disruptions in utility service can seriously affect the safety of life and property and impair the public welfare.

Put simply, operators of private systems, particulary those of the essential Energy Utilities, should not have to pay the "bypass" or "nonuse" charges due to the fact that local exchange facilities are not a comparable alternative to private facilities. The private systems of Energy Utilities do not pose a meaningful threat to the continued viability of the local telephone companies. Accordingly, in the House bill, proposed Section 221(e)(3)(B)(iii) should be modified as follows (deleted language is indicated by brackets):

"(iii) a charge reflecting the availability of the facilities of the exchange carrier for exchange access as an alternative for indirectly interconnecting interexchange carriers [and interexchange customers] to the extent such facilities are not used for exchange access by such carriers [and customers,] and

For the same reasons, proposed Section 221(e)(4)(A) should be clarified to indicate that its application is limited to entities that bypass local exchange facilities in order to provide "for-hire" services competitive with local exchange, and not private, i.e., non-common carriers systems which do not operate on a for-hire basis. This could be accomplished by adding the following qualifying statement to the end of Section 221(e)(4)(A):

"This section shall not apply to any private system operated on a not-for-profit basis that bypasses exchange facilities."

In the Senate bill, clarifying or explanatory language should be included in the Report accompanying the legislation so that private systems which bypass the local exchange are not subject to the penalty provided for in proposed Section 410(e).

B. Access Charges Should Be Cost-Based

Another area of concern in the Act relates to the assessment of access charges. The Act does not offer any guidance on which telephone lines access charges will be imposed. For example, a typical private system may involve a Private Branch Exchange (PBX) facility located on an Energy Utility's premises. A large number of inhouse station lines, *e.g.*, 100 to 1000, may be connected to this PBX to provide interconnection within the Energy Utility's premises. This PBX usually is connected to a telephone company exchange switch at the nearest central office by a number of lines which provide private exchange access to some or all of the stations on the PBX. These PBX-to-central-office lines typically provide access to the local exchanges of the exchange carrier, and also provide access to WATS and message toll services. Where private systems exist, channels which provide inter-LATA or interexchange communications are connected to the customer's premises PBX. These circuits typically are used to provide in-house communications on the customer's network and in many, if not most cases, are restricted from accessing the local exchange network through the premises PBX. In these cases, the exchange facilities are not accessed to carry traffic from the private inter-LATA or interexchange circuits. In this situation, the private system operator should not be forced to pay an access charge on the lines between the customer's premises PBX and the exchange carrier switch which are there to handle local exchange traffic only.

However, in some private systems, automatic access to the local exchange carrier is provided indirectly through the premises PBX to the local exchange for private circuits which carry inter-LATA or interexchange traffic over the central office trunks from the premises PBX to the exchange carrier's central office switch. Such access may be provided over all such trunks or over only a few.

If access charges are to be imposed, they should only be imposed on those circuits which actually carry private inter-LATA or interexchange circuits to the exchange carrier's switch. Where such access is not provided, no access charge should be imposed.

Although the logical assumption is that access charges will be imposed only on the lines which actually access the local exchange facilities rather than those which might or which have the necessary capability, such an essential determination should not be left to speculation. Clearly, the basis of an access charge is to compensate the local exchange for providing exchange access. Hence, the charges should be cost-based and limited to services actually provided and obtained.

In this regard, UTC endorses the language set forth in proposed Section 221(e)(2)(B) of the House bill which outlines access charge requirements applicable to interexchange carriers that directly interconnect with local exchange facilities. The same principles should be applied to "persons who indirectly interconnect." Also, new language should be added to clarify that access charges will be assessed only on the private system inter-LATA or interexchange lines which actually access the local exchange, not on those which merely have the capability but do not in fact do so. Accordingly, proposed Section 221(e)(3)(A) of the House bill should be amended as follows (New language is underscored):

"(3)(A) Such system shall provide that an exchange common carrier shall submit to the Commission a tariff for exchange access available from such carrier for interexchange carriers or other persons who indirectly interconnect with the facilities of such exchange carrier. *Each tariff must comply with the requirements of Section 221(e)(2)(B) and apply solely to the lines actually interconnected to local exchange facilities* for the purpose of transmission of inter-LATA or interexchange traffic.

With regard to the Senate bill, a new subsection (f) should be added to Section 221. The provision would read as follows:

"(f) For purposes of section 221(e), exchange access charges shall be assessed solely on the lines actually interconnected to local exchange facilities for the purpose of transmission of inter-LATA or interexchange traffic."

Similarly, proposed section 201(c)(1) of the Senate bill should be modified to clarify that the universal service charge would only be applied on inter-LATA or interexchange private system lines actually accessing local exchange facilities:

(New clarifying language is in italic.)

"((c)(1) The joint board established pursuant to section 410(d) of this Act shall establish a universal service charge schedule to insure that basic telephone service will be available at reasonable rates throughout the United States. Such schedule shall take effect on January 1, 1986, or on the date of the termination of the current subscriber plant factor compensation arrangement, whichever first occurs. Such schedule shall designate universal service costs to be allocated to the Federal jurisdiction and provide for their collection by means of a universal service charge that is payable *based on the number of inter-LATA or interexchange private system lines actually interconnected to local exchange facilities* by any inter-LATA carrier or any provider of inter-LATA services or private system that connects directly or indirectly to any exchange carrier or any local exchange switched network used to provide basic telephone service.

C. The Notification Provision in the House Bill is Unduly Burdensome

Section 221(e)(6)(A) of the House bill would apparently require anyone who owns or operates a telecommunication system to notify the exchange carriers, the Federal Communications Commission and the appropriate state commissions. This provision is unnecessarily burdensome and overinclusive. If, as recommended, access charges are assessed based on facilities actually used, operators of private systems should be excluded from the notification requirement.

IV. CONCLUSION

UTC recommends that the "bypass" and "nonuse" penalties be deleted from the Act. Additionaly, UTC recommends that the Act be clarified so as to provide that access charges are to be cost-based and assessed only on services actually used.

UTC greatly appreciates this opportunity to submit comments on S. 1660 and H.R. 3621 and would be pleased to discuss any aspect of these comments further, or to provide additional information. In this regard, please do not hesitate to contact our counsel, Charles M. Meehan or Shirley S. Fujimoto of Keller and Heckman at (202) 457-1100.

STATEMENT OF THE ASSOCIATION OF DATA COMMUNICATIONS USERS

The Association of Data Communications Users (ADCU) appreciates this opportunity to submit to the Committee on Commerce, Science, and Transportation its

Statement on S. 1660 and related issues concerning the preservation of universal telephone service.

I. INTRODUCTION

A. ADCU Organization and Purpose

The Association of Data Communications Users (ADCU) is the national representative for more than 175 companies and institutions which rely extensively on data communications as a cornerstone to providing quality goods and services to the public. ADCU represents a broad cross-section of companies and organizations, *e.g.*, banks, insurance companies, utilities, petroleum companies, universities, and manufacturers which produce the entire gamut of consumer products. Two-thirds of ADCU's membership consists of Fortune 500 companies, with the remaining membership constituting smaller companies and organizations with annual sales of $25 million to $50 million. Irrespective of the precise nature or size of the members' businesses, ADCU members all depend heavily upon data communications in conducting their day-to-day operations. ADCU members conduct a substantial portion of their business activities through the telecommunications network. For many of the businesses represented by ADCU, telecommunications expenditures represent a substantial cost of doing business. Hence, ADCU members are vitally and directly affected by the telecommunications policy proposals embodied in S. 1660.

ADCU members rely on private telecommunications systems, which typically are comprised of extensive intercity private line leased voice and data transmission circuits. These systems also include privately-owned and operated microwave systems, wireline telephone system, fiber optics systems, and satellite earth stations. These systems are not used to provide "for hire" or "for profit" telecommunications service to third parties. Rather, the primary reason ADCU members operate therir own private systems is to ensure complete control over the availability of quality communications transmissions. This control is particularly important because local exchange carriers are generally unable to handle ADCU members' data transmission requirements, especially with respect to bandwidth and speed.

American businesses are becoming increasingly dependent upon the use of data communications equipment, systems, and services. This trend will continue to increase in the business community as technological developments and greater efficiencies evolve. These improvements in data communications, equipment, services, and systems will not be realized, however, unless business and other users are assured of access to quality communications at reasonable rates.

II. AREAS OF SPECIFIC ADCU CONCERN

Access Charges

A. Cost-Based Access Charges

ADCU members support the payment of their "fair share" for use of exchange access facilities. To meet, however, the statutory objective embodied in proposed Section 221(e)(1)(B) of achieving "equitable treatment" of all persons who access local exchange facilities, ADCU submits that assignment of exchange access costs should be imposed on a cost-causative basis. ADCU believes that since the basis for imposing access charges is to compensate local exchange carriers for providing exchange access, the access charge tariffs must not require parties to pay for any exchange access that is not specifically provided by an exchange common carrier. Accordingly, Section 3 of S. 1660 should be amended to reflect that access charges paid by private system users are cost-based. This could be accomplished by adding the following new subsection "(f)" to Section 221 (new language in italic):

(f) *For purposes of Section 221(e), exchange access charges shall be assessed solely on the lines actually interconnected to local exchange facilities.*

This proposed amendment will ensure that private system users will not pay access charges for facilities which do not access the local network.

Furthermore, in order to promote the concept of cost-based pricing, subscribers of dedicated private lines should be exempt from paying access charges because this type of service does not utilize exchange access facilities and imposes no cost burdens on the local public switched network. Private line service offerings provided by interexchange carriers consist of transmission channels between or among points as specified by the user. As a dedicated, non-switched service, private line channels involve no marginal costs of usage. Once the private line facility is installed, there is a direct connection from the end user to the interexchange carrier, and the level of usage or loading of the channel generates no further costs to the exchange network. Since rates charged for private line service are already cost-based, exempting private line users from paying access charges would provide an efficient rate structure and facilitate efficient use of private line transmission plant.

B. Users of Private Systems That Bypass Exchange facilities Should Not Pay Access Charges

There is a growing misconception that customers bypass exchange carriers in order to avoid paying rate increases or when rates charged for the provision of service are in excess of the costs. Based on this misconception, some legislative proposals (i.e., H.R. 3621) would require users of privately-owned telecommunications systems that do not utilize exchange access facilities to pay access charges because such users often rely on the "availability" of the local telephone company as a back-up to the private systems. There is no basis for assuming that the use of private systems is interchangeable with use of local exchange service. As will be discussed, this presumption is erroneous.

The private telecommunications systems used by ADCU members are designed and operated so that users can obtain services that local telephone companies either do not now generally provide or are incapable of providing. For example, users construct privately owned and operated microwave, satellite, and fiber optics systems for the simple reason that the Bell System is unable to handle information at the speed and bandwidth necessary for data transmission on a large scale. The telephone network was designed for analog voice transmission, with a frequency bandwidth of 4000 Hertz (Hz). In transmission over the Direct Distance Dialing Network, the 4000 Hz can handle 4800 bits per second (bps) or, with some sacrifice of accuracy, 9600 bps.[1] Thus, with the widespread use of large computers and the need to transmit at high speed large amounts of data to and from databanks, use of private systems is essential to meeting ADCU members' data communications requirements.

Accordingly, the demand for and reliance on private systems is inelastic; local exchange service is simply not a viable substitute for high speed data transmissions. Use of privately-owned systems, therefore, is not a matter of choice but of necessity because exchange carriers do not have the required capabilities to handle ADCU members' data transmissions. Hence, the cost and availability of local exchange service may not be considered the primary or even a contributory factor in the utilization of private systems. Thus, legitimate concerns for protection of exchange access carriers are not involved and users of private systems should not have to contribute to the local telephone company's costs because these users cannot rely on exchange facilities as an alternative to their private systems.

Furthermore, legislative provisions that require users of private systems to pay access charges to reflect the availability of exchange access facilities will be destructive to a growing, competitive telecommunications industry and will have a chilling effect on the deployment of new technologies. Imposition of access charges on private system users will eliminate any incentive to develop and deploy new technologies. The legislation would thwart efficiency and competitive service offerings by imposing access charges for using innovative systems that do not engage exchange access facilities. Such a result would dampen technological progress and undermine the goal of fostering competition.

Based on the foregoing conceptual framework and the underlying needs of data communications users, ADCU submits any legislation enacted to ensure the availability of universal service at reasonable rates must not penalize entities that utilize private systems in lieu of exchange access facilities. The legislation should be drafted to reflect the fact that private systems are not a substitute for the availability of exchange access facilities.

UNIVERSAL SERVICE CHARGE

Section 4 of S. 1660 would amend the Communications Act of 1934 by establishing a universal service charge to ensure the continued availability of universal telephone service at reasonable and affordable rates. In order to ensure that parties pay universal service charges based only on exchange facilities that are actually used to provide exchange access, proposed subsection 201(c)(1) should be amended as follows (new language in italic):

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[1] Importantly, circuits providing the latter capacity bypass the local exchange.

"(c)(1) The joint board established pursuant to section 410(d) of this Act shall establish a universal service charge schedule to insure that basic telephone service will be available at reasonable rates throughout the United States. Such schedule shall take effect on January 1, 1986, or on the date of the termination of the current subscriber plant factor compensation arrangement, whichever first occurs. Such schedule shall designate universal service costs to be allocated to the Federal jurisdiction and provide for their collection by means of a universal service charge that is payable *based on the number of lines that actually interconnect to local exchange facilities* by any interLATA carrier or any provider of interLATA services or private system that connects directly or indirectly to any exchange carrier or any local exchange switched network used to provide basic telephone service."

ADCU also believes that the legislative provisions underlying the establishment and imposition of the universal service charges must be amended in order to carry out their intended purposes. For example, although the universal service charge is designed to provide relief to many Americans, especially the poor, elderly, handicapped, and those living in high-cost urban and rural areas, there are no assurances that the truly needy will derive any direct benefit. Importantly, there are no specific provisions or criteria to ensure that the contributions for universal service costs are disbursed to the intended beneficiaries. It should be recognized that it is more efficient to direct subsidies to individuals, not exchanges or telephone companies. Without appropriate safeguards, the legislation can also produce such anomalous results as wealthy citizens being subsidized rather than or along with the truly needy. Accordingly, the legislation must be amended to establish eligibility criteria for telephone subscribers who are subsidized by universal service charges.

ADCU is also fundamentally concerned that because the Fund provides virtually automatic compensation to BOCs with non-traffic sensitive facilities in excess of 110 per centum of the national average, it could have the adverse effect of promoting inefficient local exchange service. The absence of effective procedures and criteria will remove incentives for provision of high quality exchange service and perpetuate inefficiencies by exchange carriers. ADCU therefore believes that specific safeguards must be designed to eliminate the potential abuses that can emerge.

Exchange carriers are not defenseless against the bypass threat. They have the capacity to upgrade their network through the addition of readily available new technologies and through the integration of new concepts into their systems. Although exchange carriers have ample technological resources to combat many types of bypass, payments from the Fund may mitigate against the need to upgrade the quality of exchange service.

Furthermore, the threshold percentages used to allow an exchange carrier to receive universal service cost fail to consider situations where exchange carriers provide service to wealthy communities where the cost-of-living is in excess of 110 per centum of the national average. In such instances, although the exchange carriers are serving such high cost areas, comparisons with the national average and the need for subsidies from the universal service charges are inappropriate. If high cost areas require contributions from the universal service charge, this should be done on an exchange by exchange basis, and not according to company. ADCU believes that the legislation should be amended to account for these situations and to ensure that only intended beneficiaries are subsidized by universal service charges, if they are ultimately implemented.

UNIVERSAL TELEPHONE SERVICE JOINT BOARD

ADCU supports Section 6 of S. 1660 with respect to the composition of the of the Universal Telephone Service Joint Board. ADCU believes that the number of FCC representatives on the Board should be greater than the number of State commission representatives.

ADCU is concerned, however, that the literal language of proposed Section 410(e) as embodied in Section 6 of the Bill, could be construed to prohibit the use of any privately-owned facilities. While Section 410(e) requires "intent" to deprive exchange carriers of access charge revenues, this provision could be applicable to any entity that utilizes a private system instead of local exchange facilities. While ADCU recognizes the importance of providing penalty provisions to ensure that parties comply with the scheme of access charges devised by the Board, ADCU members should not be penalized for the considerable investments they have made in their private telecommunciations systems. Accordingly, the language of Section 410(e) should be modified to clarify that the use of private systems in lieu of exchange facilities is not illegal.

FEDERAL COMMUNICATIONS COMMISSION JURISDICTION

ADCU supports the proposal embodied in Section 5 of S. 1660 that would allow the Federal Communications Commission (FCC) to assert jurisdiction over inter-LATA telephone service. In light of the recent divestiture of the Bell System, ADCU believes that this amendment to the Communication's Act of 1934 will enhance the FCC's ability to promote the purposes of the Act and serve the public interest.

ADCU appreciates the opportunity to express its views on this important legislation and stands prepared to offer any further information or assistance to the Committee.

STATEMENT OF THE ASSOCIATION OF DATA COMMUNICATIONS USERS

The Association of Data Communications Users (ADCU) appreciates this opportunity to submit to the Committee on Energy and Commerce its Statement on H.R. 3621 and on related issues concerning the preservation of universal telephone service.

I. INTRODUCTION

A. ADCU organization and purpose

The Association of Data Communications Users (ADCU) is the national representative for more than 175 companies and institutions which rely extensively on data communications as a cornerstone to providing quality goods and services to the public. ADCU represents a broad cross-section of companies and organizatioins, *e.g.*, banks, insurance companies, utilities, petroleum companies, universities, and manufacturers which produce the entire gamut of consumer products. Two-thirds of ADCU's membership consists of Fortune 500 companies, with the remaining membership consituting smaller companies and organizations with annual sales of $25 million to $50 million. Irrespective of the precise nature or size of the members' businesses, ADCU members all depend heavily upon data communications in conducting their day-to-day operations. ADCU members transact a substantial portion of their business activities through the telecommunications network. For many of the businesses represented by ADCU, telecommunications expenditures represent a substantial cost of doing business. Hence, ADCU members are vitally and directly affected by the telecommunications policy proposals embodied in H.R. 3621.

ADCU members rely on private telcommunications systems, which typically are comprised of extensive intercity private line leased voiice and data transmission circuits. These systems also include privately-owned and operated microwave systems, wireline telephone systems, fiber optics systems, and satellite earth stations. These systems are not used to provide "for hire" or "for profit" telecommunications service to third parties. Rather, the primary reason ADCU members operate their own private systems is to ensure complete control over the availability of quality communications transmissions. This control is particularly important because local exchange carriers are generally unable to handle ADCU members' data transmission requirements, especially with respect to bandwidth and speed.

American businesses are becoming increasingly dependent upon the use of data communications equipment, systems, and services. This trend will continue to increase in the business community as technological developments and greater efficiencies evolve. These improvements in data communications, equipment, services, and systems will not be realized, however, unless business and other users are assured of access to quality communications at reasonable rates.

B. Summary of ADCU statement

ADCU prefaces its statement by noting that although it supports the concept of universal telephone service and recognizes a social need to provide such service, certain provisions of the Bill, unless amended, will erode the competitive nature of the telecommunications environment and discriminate against users of private telecommunications systems. In this regard, ADCU believes that certain modifications to H.R. 3621 are necessary to ensure to all users, including business users, the availability of a quality, reasonably priced national telecommunications network. Specifically, ADCU is proposing that H.R. 3621 be modified to ensure that owners of private systems are not penalized for using their systems in lieu of exchange facilities; access charges paid by private system users be cost based; subscribers of dedicated private lines be exempt from paying access charges; appropriate safeguards and criteria be interjected in the Universal Service Fund provisions to ensure that intended beneficiaries are subsidized and that the Fund does not promote inefficient local exchange service; and that private users who do not connect with exchange access facilities be exempted from notification requirements.

II. AREAS OF SPECIFIC ADCU CONCERN

ACCESS CHARGES

A. Why ADCU members use private telecommunications systems

The proposed legislation presumes that customers bypass exchange carriers in order to avoid paying rate increases or excessive rates. Based on these assumptions, the legislation would require users of privately owned and operated systems to pay access charges because such users in effect rely on the "availability" of the local exchange facilities as a back-up to the private systems. As will be discussed, the legislation improperly assumes that the use of private systems is interchangeable with use of local exchange service.

The private telecommunications systems used by ADCU members are designed and operated so that users can obtain services that local telephone companies either do not now generally provide or are incapable of providing. For example, users construct privately owned and operated microwave, satellite, and fiber optics systems, for the simple reason that the Bell System is unable to handle information at the speed and bandwidth necessary for data transmission on a large scale. The telephone network was designed for analog voice transmission, with a frequency bandwidth of 4000 Hertz (Hz). In transmission over the Direct Distance Dialing Network, the 4000 Hz can handle 4800 bits per second (bps) or, with some sacrifice of accuracy, 9600 bps.[1] Thus, with the widespread use of large computers and the need to transmit at high speeds large amounts of data to and from databanks, use of private systems is essential to meeting ADCU members' data requirements.

Accordingly, the demand for and reliance, on private systems is inelastic; local exchange service is simply not a viable substitute for high speed data transmissions. The use of privately-owned systems, therefore, is not a matter of choice but of necessity because exchange carriers do not have the required capabilities to handle ADCU members' data transmissions. Hence, the cost and availability of local exchange service may not be considered the primary or even a contrubutory factor in the utilization of private systems. Thus, legitimate concerns for protection of exchange access carriers are not involved and users of private systems should not have to contribute to the local telephone company's costs because these users cannot rely on exchange facilities as an alternative to their private systems.

The legislative proposal for imposing access charges on entities that do not utilize the public switched network is also contrary to the purpose clause of Section 2(b)(4) of the legislation. This provision states that the Universal Telephone Service Preservation Act of 1983 is intended "to assure that the economy, general welfare, and national security of the United States will benefit from *continuing improvements in telecommunications technology and the continued development of a competitive telecommunications industry.*" (emphasis added).

Legislative provisions that require users of existing private systems to pay access charges to reflect the availability of exchange access facilities are punitive; many private users have made large capital investments as the only means of securing reliable data transmission facilities. Moreover, with respect to *planned* facilities, imposing access charges on entities that do not utilize exchange facilities will be destructive to a growing, competitive telecommunications industry and will have a chilling effect on the deployment of new technologies. The legislation would thwart efficiency and competitive service offerings by imposing access charges for using innovative systems that bypass exchange excess facilities. Such a result would dampen technological progress and undermine the goal of fostering competition.

Based on the foregoing conceptual framework and the underlying needs of data communications users, ADCU submits that H.R. 3621 should be modified so as not to penalize entities that utilize private systems in lieu of exchange facilities. These modifications are needed to reflect the fact that private systems are not a substitute for the availability of exchange access facilities. Specifically, Section 221(e)(3)(B)(iii) should be amended to provide that users of private systems shall not have to pay a charge reflecting the "availability" of exchange access facilities. This could be accomplished by the following revision (deleted language is interlined):

Section 221(e)(3)(B)

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[1] Importantly, circuits providing the latter capacity bypass the local exchange.

"(iii) a charge reflecting the availability of the facilities of the exchange carrier for exchange access as an alternative for indirectly interconnecting interexchange carriers to the extent such facilities are not used for exchange access by such carriers and customers, and . . . ."

Furthermore, ADCU believes that the language of proposed Section 221(e)(4)(A) must be clarified to indicate that this section solely applies to commercial entitles that bypass exchange carrier facilities and does not apply to private systems that do not operate on a for-hire basis. As presently drafted, the section requires that any entity who for commercial purposes makes available facilities, services or related functions for exchange access is subject to an access charge based on the availability of the exchange carrier's facilities. The appropriate mechanism for implementing this clarification would be the inclusion of language in the Conference Report stating:

"Section 221(e)(4)(A) is intended to require those entities providing for-hire private facilities that bypass exchange carrier facilities to pay a charge reflecting the availability of the exchange carrier's facilities for exchange access as an alternative for the private facilities. For the purposes of this legislation, Section 226(e)(4)(A) shall not apply to any private system operated on a non-profit basis that bypasses exchange access facilities."

B. Cost-based access charges

ADCU members support the payment of their "fair share" for use of exchange access facilities. To meet, however, the statutory objective embodied in proposed Section 221(e)(1)(B) of achieving "equitable treatment" for all persons who access local exchange facilities, ADCU submits that assignment of exchange access costs should be imposed on a cost-causative basis.

ADCU endorses the principles embodied in Section 221(e)(2)(B) with respect to requiring that exchange common carrier access charge tariffs are justified by costs and ensuring that parties are not required to pay for any exchange access that is not specifically provided by an exchange common carrier. Accordingly, proposed Section 221(e)(3)(A) should be amended to reflect that access charges paid by private system users must be cost-based. This could be accomplished by the following revision (new language in italic):

"(3)(A) Such system shall provide that an exchange common carrier shall submit to the Commission a tariff for exchange access available from such carrier for interexchange carriers or other persons who indirectly interconnect with the facilities of such exchange carriers. *Each tariff must comply with the requirements of Section 221(e)(2)(B) and apply solely to the exchange access lines actually interconnected to local exchange facilities.*"

This proposed amendment will ensure that private system users do not pay access charges for facilities which do not access the local network.

Furthermore, in order to promote the concept of cost-based pricing, subscribers of dedicated private lines should be exempt from paying access charges because this type of service does not utilize exchange access facilities and imposes no cost burdens on the local public switched network. Private line service offerings provided by interexchange carriers consist of transmission channels between or among points as specified by the user. As a dedicated, non-switched service, private line channels involve no marginal costs of usage. Once the private line facility is installed, the level of usage or loading of the channel generates no further costs to the exchange network. Since rates charged for private line service are already cost-based, exempting private line users from paying access charges would provide an efficient rate structure and facilitate efficient use of private line transmission plant. ADCU submits that clarifying language to this effective should be included in the Conference Report.

UNIVERSAL SERVICE FUND

Section 5 of H.R. 3621 would amend the Communications Act of 1934 by establishing a Universal Service Fund (Fund) to ensure that continued availability of universal telephone service at reasonable and affordable rates. ADCU submits that the legislative provisions underlying the establishment and implementation of the Fund must be amended in order to carry out the Fund's intended purposes.

For example, although the Fund is designed to provide relief to many Americans, especially the poor, elderly, handicapped, and those living in high-cost urban and rural areas, there are no assurances that the truly needy will derive any direct benefit. Importantly, there are no specific provisions or criteria to ensure that the contibutions made to the Fund are disbursed to the intended beneficiaries. It should be recognized that if it is nore efficient to direct subsidies to individuals, not exchanges or telephone companies. Without appropriate safeguards, the legislation can also produce such anomalous results as wealthy citizens being subsidized rather than or along with the truly need. Accordingly, the legislation must be amended to establish eligibility criteria for telephone subscribers who are subsidized by the Fund.

ADCU is also fundamentally concerned that because the Fund provides virtually automatic compensation to BOCs with non-traffic sensitive facilities in excess of 115 per centum of the national average, it could have the adverse effect of promoting inefficient local exchange service. The absence of effective procedures and criteria will remove incentives for provision of high quality exchange service and perpetuate inefficiencies by exchange carriers. ADCU therefore believes that specific safeguards must be designed to eliminate the potential abuses that can emerge.

Exchange carriers are not defenseless against the bypass threat. They have the capacity to upgrade their network through the addition of readily available new technologies and through the integration of new concepts into their systems. Although exchange carriers have ample technological resources to combat many types of bypass, payments from the Fund may mitigate against the need to upgrade the quality of exchange service.

Furthermore, the threshold percentages used to allow an exchange carrier to receive payments from the Fund fail to consider situations where exchange carriers provide service to wealthy communities where the cost-of-living is in excess of 115 per centum of the national average. In such instances, although the exchange carriers are serving such high cost areas, comparisons with the national average and the need for subsidies from the fund are inapropriate. If high cost areas require contributions from the Fund, this should be done on an exchange by exchange basis, and not according to company. ADCU believes that the legislation should be amended to account for these situations and to ensure that only intended beneficiaries are subsidized by the Fund.

NATIONWIDE AVERAGING

Section 8 of H.R. 3621 would amend the Communications Act of 1934 by requiring that any interexchange tariff in effect July 1, 1983 shall be based on the nationwide average of the cost of providing interexchange service. ADCU submits that required nationwide averaging would constitute a departure from the cost based pricing which competition requires.

While the threat of bypass is generally specific to certain geographic regions and not widely diffused, the possibility of network bypass will provide some constraint on the level and structure of interexchange carrier switched and private line rates in those specific geographic areas. The threat of bypass in these areas will create pressure for interexchange carriers to deaverage their interexchange rates by route or geographic area to minimize the loss of traffic induced by averaged rates which exceed the costs of alternative point-to-point private systems. Adequate pricing flexibility will enable interexchange carriers to compete effectively and provide disincentives for bypass. Section 226, however, would eliminate any pricing flexibility and provide incentives for network bypass by requiring interexchange rates to remain artificially high in certain geographic areas.

NOTIFICATION REQUIREMENT

ADCU submits that the notification requirements imposed by proposed Section 221(e)(6)(A) are unnecessarily burdensome and should be modified. According to the notification requirement, anyone who owns communications equipment which does not directly connect with exchange access facilities shall notify the appropriate exchange carriers, Federal Communications Commission, and appropriate state Commissions. Since, as suggested herein, users of private systems that do not operate their systems on a for-hire basis should only be required to pay exchange access charges based on the exchange facilities that are actually used, such private users should be exempt from the notification requirement.

ADCU appreciates this opportunity to express its views on this important legislation and stands prepared to offer any further information or assistance to the Committee.

STATEMENT OF EUGENE F. MURPHY, CHAIRMAN, RCA COMMUNICATIONS, INC.

The RCA Communications operating companies provide many specialized services to the public including domestic satellite, high-speed data and telex services. These companies have established and operate special communications networks that, for the most part, are not interconnected to the Nation's public telephone network. They pay separate charges directly to local telephone companies for transmission facilities which connect customers to their networks.

RCA Communications agrees with the objective of universal telephone service at affordable prices. Legislation to promote this goal should be based on equitable principles, however, that protect the interests of all telecommunications users and continue to confine subsidies within the telephone industry. Communications companies outside the subsidy system that already pay local telephone companies separate rates for dedicated lines to reach their customers and that do not interconnect with telephone users should not be required to subsidize the long-distance telephone industry.

INTRODUCTION AND SUMMARY

RCA Communications, Inc. is a wholly-owned subsidiary of RCA Corporation. It exercises overall management responsibility for the operating companies in the RCA communications group—RCA Global Communications, Inc., which provides a full range of international record communications services as well as domestic telex service and private line services; RCA American Communications, Inc., which provides domestic satellite services; RCA Cylix Communications Network, Inc., which provides domestic high-speed packet-switching services; and RCA Network Services, Inc., which currently manages RCA's corporate telephone system and is engaged in developing new domestic services.

The principal offerings of these operating companies are provided over RCA-designed and operated communications networks that utilize facilities leased from local telephone companies but do not interconnect with the nation's public telephone network. For example, telex customers are linked to RCA Globcom's telex network by dedicated local loops leased by RCA Globcom from local telephone companies. RCA Globcom and Americom lease private lines from local telephone companies to provide point-to-point voice and data services. Cable television networks are linked to RAC Americom's satellite facilities by dedicated wideband facilities. Data customers are linked to RCA Cylix's high-speed packet-switching network by over 70,000 miles of leased transmission lines. In all, our operating communications companies paid approximaely $31.4 million to the Bell System for these transmission facilities in 1982.

RCA Communications does not dispute the principle that everyone in the United States should be allowed to obtain basic telephone service at an affordable price. This objective has been accomplished in the past by requiring long-distance telephone companies to subsidize local rates; regulating the rates, profits, investments and depreciation expenses of local telephone companies; improving technology and management efficiency; federal assistance programs administered by the Rural Electrification Administration; revenue contributions from Yellow Pages; and requiring that telephone companies charge cost-justified rates for facilities leased to providers of other services. The universal service goal may also be served by lifeline telephone service for the poor and handicapped, or by earmarking a portion of the federal telephone excise tax to support local telephone rates at reasonable levels.

These mechanisms permit local telephone rates to be kept at reasonable levels without forcing legislators to burden individuals and firms outside the telephone industry with subsidy payments. There is no reason to require that regulators or legislators jettison these mechanisms in the face of change. Nor is there any justification for burdening firms outside the telephone industry with the cost of facilities they do not use.

Accordingly, we strongly urge that any legislation adopted by the Committee treat all users fairly. Legislation should not require users of special communications networks that do not interconnect with telephone subscribers and whose business successes do not depend upon universal telephone service to subsidize the long-distance telephone industry by paying an access "surcharge". Cross-subsidies are inappropriate in view of the fact that our communications operating companies are already paying local telephone companies separate rates for local loops. In the current marketplace environment, the adverse consequences of establishing a cross-subsidy program also militates against requiring operators of special communications networks to pay telephone companies twice for local connecting facilities.

In particular, telex services provided by companies such as RCA Globcom and high-speed data services such as provided by RCA Cylix and RCA Americom should be excluded from any surcharge to support universal telephone service.

As Chairman Dingell stated in introducing H.R. 3621, the entire premise of the surcharge is to "insure that all who benefit from the availability of universal telephone service pay for it." Neither RCA Globcom nor RCA Cylix, each with their specialized data service, benefits from the availability of the universal telephone service. Nor, in many cases, does RCA Americom when it provides cable television, point-to-point voice, and data transmission services.

THE TELECOMMUNICATIONS MARKETPLACE

Telecommunications companies are improving services available to the public, new companies are entering the marketplace and the costs of existing services are being lowered in response to technological improvements and increased competition.

Recent regulatory and judicial actions have attempted to promote these marketplace trends. The FCC has acted in the Competitive Carrier Rulemaking and Computer II Inquiry to reduce the regulation of non-dominant common carriers and resellers of terrestrial facilities and to eliminate title II regulation of enhanced communications services and customer premises equipment. The FCC has also adopted in its MTS/WATS Market Structure proceeding a plan requiring local telephone companies to recover costs allocated to interstate services through cost-based rates charged to interexchange carriers and telephone subscribers. In addition, Judge Greene has approved the divestiture of 22 Bell Operating Companies by AT&T and required that the BOCs offer non-discriminatory access to their local exchange facilities under cost-justified tariffs.

These pro-competitive developments are significantly changing the telecommunications marketplace. However, gauging their effect on telecommunications providers, users and particularly telephone subscribers must await further development. The Congress should not rush to fashion a remedy until it can be determined what problems exist in providing universal telephone serivce at affordable rates.

This uncertainty, inevitable in such a period of tremendous change, will not be resolved until: (1) local telephone companies file exchange access tariffs with the FCC covering interstate services and tariffs with state PUCs covering intrastate services; (2) the FCC and state PUCs complete their review of these tariffs; (3) AT&T Long Lines and other interexchange carriers have an opportunity to review the tariffs filed by local telephone companies and prepare complementary tariffs for their services; and (4) Judge Greene's July 8 order—which reserves the Bell name to the BOCs, provides assurances that the costs of equal access will be borne by interexchange carriers and allows the BOCs preferential treatment in the intra-LATA toll market—is reflected in the BOCs' forecasted revenue requirements.

As these developments are being assessed, the FCC and state PUCs retain authority to regulate telephone rates. The FCC can postpone the implementation of its access charge decision and, after tariffs are filed, can suspend these tariffs for 5 months and investigate them. The FCC has also decided to create a Universal Service Fund to protect against local telephone rate increases during a transition period and has proposed a plan to monitor the effect of its access charge decision on universal telephone service. At the state level, PUCs have comparable power to defer the effectiveness of tariffs filed for intrastate service offerings. Furthermore, these regulatory agencies have authority to reject any proposed rate increase which is based on excessive allowances for depreciation, includes an unreasonably high rate of return on regualted service offerings or fails to account for the substantial revenue from Yellow Pages advertising.

Accordingly, there are substantial safeguards that regulators may still use to preserve universal telephone service. The Congress should afford these mechanisms a chance to work and then act only if it becomes clear that they are incapable of protecting the public interest in universal telephone service.

SPECIAL COMMUNICATIONS NETWORKS

If the Congress nevertheless choses to enact legislation, it is critical that the interests of all telecommunications users be protected. These users include, in addition to telephone subscribers, individuals and firms who depend on specialized communications networks for many services such as telex, point-to-point voice, cable television programming and high-speed data.

The RCA operating communciations companies serve such non-telephone user groups. For example, RCA Americom transmits cable television programming by satellite to more than 6,500 receive-only earth stations throughout the country, which serve approximately 30 million of the Nation's households. RCA Cylix provides a dedicated high-speed packet-switching service nationwide among 100 user locations over point-to-point and multipoint leased telephone company facilities and satellite data links. RCA Globcom provides telex service to approximatley 9,000 customers concentrated in major metropolitan areas, who primarily depend on the service to meet their domestic and overseas communications requirements.

The communications networks that our operating companies have established to provide these services to the public are different from the networks of many others telecommuntications providers in important respects. Unlike many independent long-distance carriers, which simply pick up and drop off traffic at the door of local telephone companies, the RCA operating communications companies already pay local telephone companies separate charge dedicated local transmission facilities terminating at customer premises. These facilities connect customers directly to the special communications networks of our operating companies. Moreover, our primary service offerings are not interconnected to telephone switching systems and cannot be transmitted to telephone subscribers. More specifically:

1. *RCA's networks are not interconnected to the switched public telephone system.* Cable television programming, point-to-point voice, high-speed packet switching and most telex calls are not transmitted over the switched public telephone network. These services are transmitted over special communications networks composed of dedicated customer access lines leased from local telephone companies, specialized central office facilities, transmission lines to earth stations and satellite links. For the most part, the users of these networks cannot use these facilities to access local telephone company switching systems. Any switching is provided within these special purpose networks by RCA-owned and operated facilities. On account of these operating characteristics, the value of our service offerings do not depend upon universal telephone service.

2. *RCA's networks serve unique customer requirements.* A majority of the communications services our operating companies provide are non-telephone services that are simply incapable of being transmitted over the public telephone network. The public telephone network was not designed to provide these services, and the technical characteristics of the public switched network are fequently incompatible with the transmission requirements of these services. Some of these services require separate facilities capable of broadband transmission, are conditioned to satisfy more precise tolerances than voice traffic and are able to perform special switching functions. It is the inability of local telephone companies to meet the specialized needs of our customers that has forced them to look to us for service alternatives not offered by telephone companies.

3. *RCA pays separate rates for local facilities.* The RCA operating communications companies lease transmission facilities from local telephone companies—we do not "bypass" local facilities. These facilities include private lines that connect a customer's telex machine to RCA Globcom's central office and facilities linking customers to RCA Americom operating centers. Presently these leased facilities are provided under tariffs on file with the FCC that are separate from tariffs covering switched telephone service, include no telephone company switching and do not provide any subsidy for residential telephone rates. The charges for these facilities, which were established by negotiation between AT&T and the other common carriers in CC Docket No. 20099 (52 FCC 2d 727), may be increased by AT&T if it chooses to file economic cost-support data with the FCC.

To summarize, customers use the networks of our operating companies to meet unique communications requirements that cannot be satisfied by the public telephone network. Providers of these services have invested substantial amounts of capital to meet the needs of their customers—not to bypass the public telephone network. Furthermore, where our operating companies obtain facilities from local telephone companies, they pay separate charges for the facilities.

THE INTERESTS OF SPECIAL NETWORK USERS

The proposed legislation requires users of special communications networks to pay into a fund that will subsidize high-cost local telephone companies and the local telephone rates charged by these companies to residential customers.

Section 4(c)(1) of S. 1660 levies a Universal Service Charge, over and above the access charge, on interLATA carriers, providers of interLATA services and private systems that connect directly or indirectly to any exchange carrier. Under section 4(c)(2) of the bill, these charges will be paid to exchange carriers to defray their costs for basic telephone service exceeding 110 percent of the national average.

To a similar effect, section 4(b) of H.R. 3621 requires interexchange carriers that interconnect directly with exchange carrier facilities, and interexchange carriers and other persons who indirectly interconnect with these facilities, to pay a Universal Service Fund surcharge. These surcharges will be disbursed from the Fund to exchange carriers whose costs for customer access lines exceed 115 percent of the national average.

In our judgment, implementing such a proposal in its present form will cause enormous public harm. It will place a substantial subsidy burden on a relatively small and embryonic segment of the telecommunications market—*i.e.*, innovators that operate in a highly competitive market and whose estimated $7 billion revenues are dwarfed by the $60 billion revenues earned by the local telephone industry, which has a 100-year monopoly and relatively stable business. Moreover, this subsidy will impact telecommunications firms that were not responsible for incurring telephone subscriber-related costs in the first place, that do not receive any benefit from the subsidies paid to local telephone companies, that do not stand to gain from universal telephone service, and that will not fall if universal telephone service is not provided. Apart from failing to contribute meaningfully to universal telephone service, such a burden will have serious adverse consequences.

The interests of special network users deserve protection. They should not be allowed to become the innocent victims of a dispute over the precise mechanism by which long-distance telephone carriers and local telephone companies pass on to end users the costs of the public telephone network. Special network users should not be forced to cross-subsidize the long-distance telephone industry for the following reasons.

1. *Cross-subsidies will harm special network users.* Users of special communications networks are no different than telephone subscribers, including many individuals and small businesses throughout the country. Indeed, in virtually all cases special network users are also telephone subscribers. A majority of these users is no better situated to pay more for service than people who subscribe only to telephone service.

2. *Cross-subsidies may eliminate existing services.* The price at which a service is available affects demand for the service, in that higher prices slacken demand and escalating prices extinguish demand. These principles apply to the non-telephone communications markets with greater force than the telephone industry. Telephony has enjoyed a 100 year headstart over other means of telecommunications and has become an essential utility in the American culture. Accordingly, while specific trade-offs will vary with pricing actions in each market, it is a fair conclusion that costs cannot be transferred to the specialized communications industry without damaging disproportionately the availability of service in the specific telecommunications market that is ultimately burdened with these costs. More importantly, even if such a trade-off is considered, the sheer magnitude of the costs that must be transferred in order to provide meaningful relief to telephone subscribers is so large that there is a substantial risk of extinguishing demand entirely in the burdened market. Such an occurrence is clearly against the public interest because it removes from the marketplace services for which a need has been demonstrated.

3. *Cross-subsidies will jeopardize investment.* The telephone industry is huge by any standard, especially when compared to non-telephone communications markets. The domestic telephone industry is populated with more than 1,400 common carriers serving over 180,000,000 telephones nationwide. Industry operating plant is valued at approximately $130 billion, operating revenue exceeds $63 billion a year and operating expenses are more than $40 billion. By comparison, less than 10 common carriers serve approximately 200,000 telex terminal locations, operate plant valued at $2.1 billion, receive roughly $1.36 billion in operating revenue and incur operating expenses of about $870 million. The packet-switched data market and many other markets served by our special communications networks are even smaller than the telex market. Even in combination, these specialized markets are dwarfed by the telephone industry and are too small to bear a significant portion of telephone industry costs. Were such costs to be loaded onto special networks, the investment in these networks would be affected adversely.

4. *Cross-subsidies will handicap new technology and services.* The development of new technology and services requires capital expenditures. The decision whether to invest capital in a particular project is based on the prospects that the project will generate sufficient revenue to recover its costs and return a reasonable profit to the investor. Since the legislation will increase the operating cost of special communications networks—which serve as testing grounds for new technologies and services—in the future these networks will attract less capital. Restricted capital availability will make it more difficult to develop new technology and services within the

United States to meet our Nation's future communications needs. The legislation therefore handicaps the entrepreneurial activity of telecommunications firms in this country when competing with other firms and with foreign corporations, which frequently receive, rather than pay, governmental subsidies.

5. *Cross-subsidies will promote uneconomical telco investment.* The subsidy plan under consideration will promote uneconomical investment decisions by local telephone companies if the Congress legislates that special network users must cross-subsidize facilities that serve other users. Local telephone company executives will no longer have financial incentives to control these costs, but will instead have incentives to transfer increased costs onto these non-users. Such a cost transfer program would be attractive to telephone company management on two grounds: first, it would not impair the already non-existent demand from special network users for telephone service; second, it would permit telephone companies to subsidize their competitive services. Absent marketplace forces, the only way to assure executives make economical investment decisions is to subject them to close regulation. But regulation of telephone company investment and profits has been proven in the past to be an inadequate substitute for marketplace forces.

CONCLUSION

The telephone industry is changing from a monopolistic, highly regulated market to a more competitive market. Competition is being promoted by new entrants, FCC regulatory action and the AT&T divestiture. These changes will affect telephone customers, but several pending regulatory matters must be resolved before the effect on local telephone rates can be measured.

The regulatory agencies will continue to regulate telephone rates during this transition period. In addition, the FCC has established a Universal Service Fund to protect telephone subscribers and intends to monitor the effect of these changes on universal telephone service. Thus, the need for legislation now is questionable.

If the Committee does consider legislation, it should protect the interests of individuals and firms who use special communications networks. These users obtain non-telephone type services over specially constructed networks that, while constituted of telephone company facilities, do not interconnect with telephone subscribers. They are not an appropriate source of revenue for a telephone subsidy fund because they are a fraction of the size of the telephone market, have communications needs that cannot be served by the public telephone network and already pay separate charges for local facilities leased from telephone companies.

Under these circumstances, we strongly urge that the Committee not require special communications network users or providers to assume additional costs of the local telephone companies. Since there users already pay separate charges for local facilities, they should not have to pay an additional surcharge to subsidize high-cost telephone service to persons with whom the users of these specialized networks cannot communicate.

STATEMENT OF THE ASSOCIATION OF AMERICAN RAILROADS

The Association of American Railroads ("AAR") is pleased to have this opportunity to present its opinions to the Senate Committee on Commerce, Science and Transportation and the House Committee on Energy and Commerce on S. 1660 and H.R. 3621, entitled the Universal Telephone Service Preservation Act of 1983. As explained below, these Bills would have a significant adverse impact on our country's railroad operations by imposing unwarranted charges on private communicaitons system that are integral to those operations. To avoid this inequity, the railroads urge that their communications systems be exempted from the universal service surcharges and bypass penalties of these Bills, and the penalty in H.R. 3621 levied against communications systems that "indirectly" interconnect to the telephone exchange.

I. BACKGROUND

AAR is a voluntary unincorporated, nonprofit organization composed of member railroad companies which, collectively operate approximately 97 percent of this country's trackage. AAR represents its member railroad companies in a wide range of concerns common to these companies, including such matters as communications, signaling, research, operations, safety, and federal legislation and regulation. In acting on behalf of its membership AAR strives to promote and maintain a safe, adequate and efficient railroad service for the public.

AAR's concerns over S. 1660, H.R. 3621 and similar pending Bills can be understood best by presenting a brief sketch of the use of communications systems by railroad companies in support of their quite complex rail transport operations.

This country's railroads have operated their own private communications systems for over 80 years. Often, throughout that period and even today, railroad private communications systems have been installed either because telephone companies did not desire to provide or could not provide the railroads with type of service required for safe and efficient rail operations.

Today, the railroads operate approximately 50 percent of the private microwave systems in this country. The total length of the private microwave systems operated by the railroads is about 44,000 route miles. This system of microwave communications consists, largely, of radio communication paths that extend between railroad offices and terminals and, therefore are beyond telephone exchange boundaries. In addition, the private microwave systems used in support of rail yard activity consist of short radio links use for such purpose as coordinating the movement of rail cars in and around terminals.

The railroads also operate wireline communication systems extending into terminals and along trackage right-of-ways. The railroadws utilize wireline communications to such a great extent in support of rail operations that many of the individual railroad wireline system are larger than many rural telephone companies. At this time, it is impossible to determine with any reasonable or reliable precision how many miles of wireline circuitry is operated by this nation's railroads. However, the use of wireline circuits by the Southern Pacific Railroad provides a good example of the reliance of our nation's railroads on private wireline communications systems. The average Southern Pacific switching yard is laced with about 100 miles of cable. This cable is not interconnected to a telephone company exchange and it generally is not available from telephone companies. It can transport high capacity digital information used for such operational purposes as car location. Additionally, Southern Pacific has about 3,500 miles of pole-strung wire used for operational communications. This wire gradually is being replaced with microwave cable.

Virtually all railroads use interconnected mobile radio systems in the operation of their trains, yards, terminals, and on their rights-of-way. Mobile radio is used extensively for such safety related functions as monitoring train safety indicators, and controlling train speed and train braking.

The private commucations systems operated by the railroads perform functions vital to the safety and success of rail operations. In fact, communications is to the railroad industry what the nervous system is to the human body—a support system necessary to the smooth functioning of the whole system. In many respects, the railroad communications systems stand in place of the flagman, who once controlled the movement of rail cars to ensure safety and efficiency. Examples of the use of railroad private communications systems include.

(a) the transmission of coded signals for use with various types of train control systems, including signalling devices;

(b) the transmission of information concerning the temperature of the journal bearings (hot box detectors) and indications of dragging equipment;

(c) radio control links connecting dispatchers with train radio systems;

(d) Private line dispatcher systems;

(e) various types of public address and annunciator systems;

(f) emergency voice communications hot lines;

(g) the transmission of data concerning and for control of car movements; and

(h) various types of data collection and distribution systems.

When one considers the complexity of a rail yard, the vast distances that rail cars may travel, and the fact that it takes two or more different rail companies to hand the majority of rail shipments from origin to destination, it becomes readily apparent that the railroads, to a much greater degree than any other transportation system, must have immediately available, reliable and redundant communications systems to promote efficiency and safety. To state that rail operations involve potential dangers is an understatement. The cost to society of the infrequent rail disasters requires no elaboration. The railroad industry's private communications system is just as essential to minimizing the potential for rail accidents as sound roadbeds and well maintained rolling stock.

Notably, the location of railroad private communications systems and the capabilities required of these systems are such that the railroads often cannot consider utilizing the facilities of telephone companies as a substitute for private communications systems. Much of the railroad private communication system mileage is located in rural areas and along rural trackage paths that are unserved or not adequately served by telephone companies. Even if substitute telephone company service were available along those paths, telephone companies largely are unable to offer a quality of service, redundancy and a rapidity of service restoration required of railroad communications systems in order to efficiently and safely manage car movements. For example, even a quite brief loss of a railroad communication path can bring railroad terminal operations to a halt and endanger lives and property. The need of the railroads for their private communications systems can be illustrated by the costs railroads incur in installling their communications systems. While the Bell System microwave bears an equipment installation cost of about $12 per channel mile, the railroads spend about $21.50 per channel mile to install their communications equipment. Yet, in the opinion of the railroads, the burden of the disproportionate investment is justified by the need to ensure safety, efficiency and reliability in railroad operations.

Congress has recognized the vital importance and complexity of maintaining safe railroad operations. Title 45 of the United States Code contains no less than 40 sections dealing with rail safety that stand as testaments to the great complexity involved in safely conducting railroad operations. Moreover, Section 303(k) of the Communications Act of 1934 vests the FCC with power to exempt certain railroad radio stations from its regulations. 47 U.S.C. § 303(k) (1976).

Again, Congress has recognized the need to promote efficient railroad operations in the Staggers Rail Act of 1980, 94 STAT. 1896. Section 2 of that law finds that railroads, historically, have been an "essential factor in the national transportation system," but that the earnings of the railroads "are the lowest of any transportation mode and are insufficient to generate funds for necessary capital improvements." Section 2 continues by finding that by 1985 the capital shortfall of the railroad industry will be between 16 and 20 billion dollars, resulting "in either further deterioriation of the rail system or the necessity for additional Federal subsidy." On the basis of these findings, Section 3 of the Staggers Act seeks to rehabilitate the rail system and assist it in obtaining needed financing "so as to preserve a safe, adequate, economical, efficient, and financially stable rail system. . . ."

With this background in mind, AAR submits that Congress would be remiss to enact any law that disrupts, prohibits, or places costs not based on service actually received on railroad private communications systems. S. 1660 and H.R. 3621, however, would so affect the private microwave systems so essential to the safety and efficiency of rail operations.

II. DISCUSSION

S. 1660 would establish a scheme of telephone exchange access charges that would (1) compensate the exchange telephone company for the cost of providing exchange access, Section 221(e); (2) assess against common carriers and private communications systems that utilize exchange facilities a surcharge to subsidize unprofitable exchange telephone companies, Section 201(c)(1); and (3) prohibit, in effect, the operation of communications systems that "bypass" the local exchange through the sanction of a $100,000 fine, Seciton 410(e).

H.R. 3621 would establish a scheme of telephone exchange access charges that would (1) compensate the exchange telephone company for the cost of providing exchange access, Section 221(3)(2)(A) and (3)(A); (2) assess a penalty payment against communications systems that interconnect with the telephone exchange at a nontoll switching office, Section 221(e)(A); (3) assess a penalty payment against the "interexchange carrier or other person" who "for commercial purposes" provides access to an exchange area without interconnecting with the telephone exchange carrier's facilities, Section 221(e)(4)(A); and (4) assess a surcharge against those who interconnect to the telephone exchange to subsidize unprofitable telephone exchange carriers, Section 221(e)(2)(C) and (3)(B)(iv).

In the opinion of AAR, the above-summarized legislative proposals would unduly harm established railroad private communication systems that are so vital to safe and efficient railway operations.

First, S. 1660 would force interconnected railroad private communication systems to pay a "universal service charge," in addition to a cost-based service charge, to subsidize unprofitable local telephone exchange carriers. Under H.R. 3621, railroad private communications systems interconnected to telephone exchange systems would pay a "surcharge" for the "Universal Service Fund," assuming that interexchange private communications systems are encompassed with the term "interexchange carrier." Presumably, the subsidy funds created by those surcharges would be used to ensure the continued, universal availability of basic, switched voice communications in the telephone exchange. In the opinion of AAR, the costs of these subsidies should be borne by those whose communications systems employ exchange access and in proportion to their relative amount of exchange use. Further, AAR believes that the costs of such subsidies should not be borne by communications systems that employ exchange access for purposes other than switched voice communication with points in the accessed exchange. Moreover, AAR believes that it is uneconomic and inequitable to now call upon those who do not provide an MTS/WATS equivalent service to contribute to a subsidy used to defray the cost of MTS/WATS equivalent service exchange access, when they have not been needed to do so in the past to ensure universal telephone service.

In this connection, Section 2(b)(2) of the H.R. 3621 states that one purpose of the Bill is: "to assure that the costs of maintaining such availability of services are *equitably allocated* among all users and providers of communication services who benefit from the availability of such services. . . ." (emphasis supplied).

An subsection (b) of that Section addresses "telephone service," it is assumed that the "services" referred to in the above-quoted subsection of Section 2 are the basic, switched voice local and long distance services equivalent to MTS/WATS. Similarly, Section 2 of S. 1660 gives as one of its purposes: "assuring that all providers of telecommunications services bear an *equitable* share of the costs of providing universal basic telephone service." (emphasis supplied).

To require private telecommunications systems—which are not substitutes for MTS/WATS and whose functions could not be adequately replaced with MTS/WATS—to bear the costs attributable to basic switched telephone service is anything but assuring that the costs of basic telephone service are "equitably allocated," or, to use the terminology of S. 1660, this requirement is hardly "equitable." These Bills, thus, are at variance with their fundamental purposes to the extent that private telecommunications systems *not interchangeable with MTS/WATS service equivalents* are forced to subsidize basic telephone service. The FCC has recognized the equitable principle that only those involved in MTS/WATS equivalent activity should be forced to subsidize this type of activity. In both its *Memorandum Opinion and Order* on reconsideration and its *Third Report and Order* in CC Docket No. 78-72, the Commission determined that it is inappropriate for private line users to pay a surcharge to subsidize the offering of basic telephone service, unless the private line is used as an alternative to MTS/WATS service. *FCC News Release,* Mimeo 5594, at 3 (July 27, 1983). It is even more evident that private microwave and wireline should not be compelled to contribute to the support of MTS/WATS activity.

Many railroad private communications systems interconnect to telephone exchanges for various purposes in support of rail operations. Many of these "private lines" are utilized merely to access discrete, preselected points in a telephone exchange, and many of these "private lines" are used to carry data essential for safe and efficient rail operations. Under S. 1660 and H.R. 3621, these interconnected systems would pay a surcharge to subsidize basic telephone service, even though they employ exchange access for a wholly unrelated type of communication. Railroad private communication systems basically are *operational* communications systems used *in support of mobile transport activity.* So understood, railroad private communications systems are nothing like MTS/WATS or basic telephone service, and certainly should not be burdened with the costs of maintaining basic telephone service.

Moreover, placing a basic telephone service subsidy surcharge on interconnected railroad private communications systems is an act of interservice cross-subsidization flowing from the generally unprofitable railroads to unprofitable exchange telephone companies. That would not be an economically rational requirement, or a very prudent financial choice, and would be at cross-purposes with the Staggers Act which found *the railroads in desperate financial condition and whose purpose was to assist the railroads and bring their earnings to an adequate revenue level. See* Section 3, P.L. 96-448. Notably, the Interstate Commerce Commission, in a recent determination, found that not a single railroad was earning adequate revenues. Any subsidy should derive from a source capable of paying the subsidy. One such source, as Congress has recognized, is not our country's railroads.

AAR is unable to determine from either S. 1660 or H.R. 3621 just how much additional cost the surcharges these Bills would create would place on railroad communications systems. These Bills are too vague in regard to computing the amount of the surcharge for AAR to develop a reasonably reliable cost to its member railroads. Nevertheless, AAR can state with assurance that this cost will be great and detrimental to the maintenance of safe, efficient railroad operations competitive with other modes of transportation. The costs associated with the concerned surcharge must be passed along to the shipper, where the market will permit, without increasing the value of the transportation service offered.

Accordingly, AAR suggests the amendment of S. 1660 and H.R. 3621 by adding the following sentence to the end of subsection (c)(1) of Section 201 of S. 1660 and to the end of subsection (a) of Section 225 of H.R. 3621:

"No such surcharge shall be charged for exchange access for any private communications system used by a railroad company, or group of railroad companies, for the support of rail operations."

Second, AAR objects to the exchange "bypass" penalties that these Bills would assess against railroad private communications systems. Section 410(e) of S. 1660 would go so far as to outlaw bypass systems through $100,000 fines. Section 221(e)(4)(A) of H.R. 3621 would assess an undetermined "bypass" penalty against railroad private communications systems that do not interconnect to an available exchange telephone system. That penalty applies to "other persons," which presumably includes railroads, who make "available . . . [communications systems] . . . for exchange access." Possibly, private railroad communicaiton systems would be regarded as made vailable to railroads for exchange access.

In the opinion of AAR, those "bypass" penalties are anticompetitive, incompatible with the needs of the railroads for communications capacity, and place monopoly, and its inherent inefficiencies, above the legitimate safety and effficiency needs of the railroads.

The concerned "bypass" provisions, in practice, would outlaw many of the railroads' private communications paths, require the railroads to seek telephone exchange facilities as a substitute, and force the railroads to interconnect communications systems having functions that do not require exchange access. The S. 1660 "bypass" provision would force the railroads to abondon, under threat of a heavy fine, many communication systems that are specifically designed to support transportation activity or which must be quickly restored to service upon breakdown, even though telephone company service is not an acceptable substitute. H.R. 3621's "bypass" provision operates somewhat differently than its S. 1660 counterpart provision, but not without unjustified negative ramifications for railroad private communications systems. For example, "exchange access" is defined in Section 3(hh) of the Bill as access "for the origination or termination of interexchange communication." This definition of exchange access is so broad that a private communications link running the 2/10 of a mile distance of the railway bridge adjacent to the 14th Street Bridge, because it spands two exchanges, would be an interexchange system, which either must access both the available local loop in northern Virginia and the District of Columbia, or pay to both "bypassed" exchange carriers a speculative charge "reflecting the availability of the exchange carrier's facilities." In other words, many private communications links would be required to be routed, unnecessarily and circuitously, through telephone company switching offices (toll switching offices in the case of H.R. 3621, see Section 221(e)(2)(A)), or pay a penalty. That result would be inefficient and counterproductive.

Section 221(e)(4)(B) of H.R. 3621, unlike S. 1660, provides railroad private communications systems with a means to avoid this bypass penalty, where "comparable facilities, services, or related functions are not available from the exchange carrier involved." That escape clause, however, is inadequate, in that it (1) presumes a bypass system should be penalized, (2) places the burden of proof on the private system owner, and (3) utilizes the standard of comparability, which is extremely subjective and will tend to impede efforts to remove non-"bypass" private systems from the burden of the penalty.

AAR does not understand the need to unnecessarily utilize local exchange facilities. The bypass penalty is injurious to beneficial private communications systems, and even worse, encourages the inefficient operation of exchange telephone companies by removing private communications systems as an alternative to telephone exchange access that forces the exchange carrier to strive for efficiency in operation and maintain low, yet compensatory, rates. Notably, the FCC created the private microwave service in its decision styled Above 890 Mc, 27 F.C.C. 359 (1959), because of a problem that the bypass penalty would risk recreating. In particular, prior to Above 890 Mc, telephone companies often would refuse to offer service if there were not adequate facilities already in place to fill the order. 27 F.C.C 2d at 413. Further, the sevice provided by common carriers, often, was not what the users wanted, insofar as the users required "better control and flexibility for meeting their own hour-by-hour operational and administrative needs." *Id.* With the "bypass" provisions in S. 1660 and H.R. 3621, Congress would only penalize private communications systems for doing what telephone companies are unwilling or unable to do as efficiently as a private communications system.

Accordingly, AAR suggests the amendment of Section 221(e)(4)(A) of H.R. 3621 by inserting the following phrase between the comma, after the word "purposes" and the word "makes": "except private railroad communications systems,".

AAR suggests the amendment of Section 410(e) of S. 1660 by inserting the following phrase after the word "manner": "except by means of a private railroad communications system,".

Third, AAR questions whether it is wise to assess a penalty payment against those communications systems that employ "indirect" interconnection to the local exchange. Section 221(e)(3)(B)(iii) of H.R. 3621 would assess a penalty for "indirectly interconnecting"; defined as interconnection to the local loop at facilities not specifically designed for exchange access. *See* Section 3(ii). Presumably, indirect local loop access is interconnection at any switching office, except for a Class 4 (toll) switching office.

In AAR's opinion, that penalty seeks to dictate to the local telephone company and communications system owner how to most efficiently utilize local loop facilities. Its premise is that local loop access through the Class 4 (toll) switching office, in all cases, is a more efficient use of the local loop. This premise, in many instances, is true. MTS/WATS type services need local loop features that are available to these services only if they are interconnected to the local loop at the Class 4 (toll) office. That premise, however, is not generally true with respect to services that are not MTS/WATS type services. For example, a review of cellular mobile radio applications filed by telephone companies reveals that these companies, with few exceptions, prefer to interconnect their proposed cellular mobile radio systems to the local loop on the trunk side of Class 5 (end) switching offices. Private line systems, in addition, often can more efficiently utilize the local loop by interconnecting on the line side of the Class 5 (end) switching office. In short, the concerned penalty provision could act, in many cases, to discourage the most efficient and best use of the local loop. In the opinion of AAR, the indirect interconnection penalty places the shoe on the wrong foot. Often, telephone companies have denied to entities seeking local loop access the most efficient and suitable form of interconnection for reasons other than a concern with efficiency. The indirect interconnection penalty provision wrongly implies that "indirect" local loop access has been forced upon the telephone company by the customer and is inefficient. Accordingly, AAR believes it would be best to remove this penalty provision from H.R. 3621 or, alternatively, to amend this provision to require telephone companies to provide interconnection that gives the customer the services the customer desires.

III. CONCLUSION

In summary, AAR requests that the Committees amend S. 1660 and H.R. 3621 by exempting railroad communication systems from any surcharge designed to subsidize unprofitable telephone companies, by exempting railroad private communications systems from the "bypass" penalty, and by deleting the provision in H.R. 3621 for charging a penalty payment against those communications systems that indirectly interconnect to the local telephone exchange.

AAR hopes that these comments prove useful to the efforts of the Committees to craft Bills that reflect a knowledge of and sensitivity to the various subtle problems involved in establishing a scheme of exchange access charges. Particularly, AAR urges the Committees to ensure that S. 1660 and H.R. 3621 remain fair to this country's railroads and to amend these Bills so that they fairly address the quite unusual situation of the railroads.

Statement of Rufus L. Edmisten, Attorney General, State of North Carolina

As Attorney General of North Carolina I am charged with the duty of representing the public interest of the State's consumers. The importance to the public of the matters now before you cannot be overstated. The long-standing public policy of universal telephone service, first expressed by Congress nearly fifty years ago in the FCC Act, is in grave danger. Congress is the best single hope that our citizens now have to keep affordable service from being washed away by the tide of ever increasing local rates.

For the past eighteen months my office has acted on behalf of consumers in many forums in an effort to assure preservation of universal service. We have urged the United States Department of Justice to recognize the negative impact of the AT&T divestiture decision on local rates and to take an active position consistent with that view. We have filed documents in opposition to the access charge in the divestiture case. We have filed comments before the FCC in hopes of stopping these unfair access charges from being foisted upon the public. We have intervened in the FCC's investigation of the impact of federal actions on local rates and services. Of course, we will continue to pursue every avenue available to us to protect the public from this catastrophe. But my experience over the last year and a half has led me to believe that in the federal courts and the regulatory agencies the course has already been set.

We are at a crises point. Though, we are currently wrestling with these same issues before our Utilities Commission, the impact of these federal decisions is overwhelming. Without Congressional action now there is little hope that we can maintain universal telephone service at reasonable rates in this nation.

Before addressing the issue of long distance access charges directly, I believe some comment on related issues is necessary to put our concerns in perspective. Access charges cannot be viewed or understood in a vacuum; they must be viewed against the backdrop of unprecedented rate requests nationwide.

In North Carolina Southern Bell has a pending rate request of one hundred and forty four million dollars. If granted, this increase would result in a fifty seven percent increase in basic residential rates and a thirty eight percent increase in basic business rates. The justification given by Southern Bell for these requested increases are divestiture and the FCC depreciation decision. The public's belief that divestiture is a threat to affordable local phone service is a direct result of these and similar statements by the phone companies, and not, as AT&T would have this committee believe, the result of gross public misperception of what has been going on in the communications industry.

In the face of these monumental rate requests nationwide—which were detailed in Representative Dingell's remarks in the Congressional Record dated July 25, 1983—consumers are also being asked to finance the local component of long distance service through "access charges". While these costs on the federal level are initially low, the projected increases in the next few years, when coupled with the increases being sought at the local level, might well be the death-knell of universal service.

Additionally, the spectre of local by-pass—whether real or imagined—has created unbelievable pressure on the state regulators to march in lock-step with the FCC and tack an additional "access charge" for intrastate long distance service on the local user. The telephone companies have thus sought to assure their financial success by what amounts to a universal telephone tax while seemingly ignoring the many revenue generating possibilities that both deregulation and new technology offer.

The questions which the American people are asking of Congress are these:

1. Should the public policy of the United States continue to be universal, affordable telephone service?
2. Are we going to allow the financial burden of the telephone communications revolution to be saddled on the local user in order to accommodate and benefit AT&T and the other long distance carriers?
3. Are the long-line companies going to be subsidized while lip service is paid to free enterprise and competition?

The answers being given to consumers by the telephone companies and the FCC are clear: Local consumers are being forced to absorb monumental rate increases to subsidize the local component of long distance service. If this decision is allowed to stand, the long-standing public policy of universal service, mandated by Congress, will be destroyed and replaced by a policy that honors technology at any cost. We must recognize that this is a public policy decision which will fundamentally effect the way we as Americans live.

The legislation now pending before Congress clearly demonstrates that we need not choose between the public policies of universal service and technological development. Technological development has always been part of the system and will continue to be so. In our view those who will most directly benefit from the use of these improvements should pay for them. If the interstate access charges are paid to the local phone companies by the long distance carriers—as Judge Green himself envisioned—the threat to universal service would be lessened, fewer consumers would need life-line service, and free enterprise and competition would be better served.

I thank the Committee for this opportunity to address these issues.

LEHMAN BROTHERS KUHN LOEB, INC.,
New York, N.Y., July 25, 1983.

Hon. BOB PACKWOOD,
U.S. Senate, Chairman, Committee on Commerce, Science, and Transportation, Washington, D.C.

DEAR SENATOR PACKWOOD: The following brief remarks summarize my position with respect to S. 1660. I would ask that these comments be included in the hearing record and, should the hearings be extended, that I be permitted to present my views in person.

When I testified before your committee in 1981, I was a strong supporter of the need for legislation and of the principles embodied in S. 898. In contrast, I believe that S. 1660 represents a precipitous action to overturn the FCC access charge decision that is both inappropriate and dangerous. Its passage would reverse a lot of hard work done by both Congressional staffs over the past six years; could disrupt the AT&T divestiture process; and would be unsettling to both the telecommunications industry and the investment community.

The FCC access charge decision of December 1982 represents a reasoned approach to a complicated problem. In particular:

1.

1. The reassignment of non-traffic-sensitive costs to the local rate payer is both economically sound and necessary in an increasingly competitive environment;

2. The phased-in approach is designed to avoid sudden dislocations in user rates, yet to be fully implemented by a time that local network bypass could become a serious problem to the local telephone companies; and

3. The absolute dollar increases in fixed telephone charges are hardly excessive when compared with recent increases in other utility rates or when considered in light of the historically declining real costs of telephone service.

As Congress knows full well, the restructuring of any industry is a complicated process. The introduction of competition and deregulation into the telecommunications industry has already produced a wealth of new products and services. The process, which Congress has been studying and supporting, is working, but cannot be accomplished without some tradeoffs.

The actions taken by the FCC, in their access charge decision, reflect these tradeoffs and are guided by the extremely tight time schedule imposed by the AT&T divestiture. I would fully expect the FCC decisions to be fine tuned in the future to reflect changing market conditions and policy objectives set forth by Congress. At this point in time, however, I would suggest that Congress accept the FCC access charge decision as a balanced approach to a needed industry pricing reform and to forbear from imposing a hastily conceived solution of its own.

Sincerely,

WINSTON E. HIMSWORTH,
First Vice President.

LEHMAN BROTHERS KUHN LOEB, INC.,
New York, N.Y., July 25, 1983.

Hon. TIMOTHY E. WIRTH,
Chairman, Subcommittee on Telecommunications, Consumer Protection, and Finance, House of Representatives, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN WIRTH: The following brief remarks summarize my position with respect to H.R. 3621. I would ask that these comments be included in the hearing record and, should the hearings be extended, that I be permitted to present my views in person.

As you may remember from the briefing I gave your subcommittee in 1981, I am a strong supporter of the need for legisaltion to establish policy and to help guide the regulators through the maze of tradeoffs implicit in the restructuring of the telecommunications industry. In my opinion, however, H.R. 3621 does not reflect a well reasoned approach to Congressional policy making. Instead, by overturning the FCC access charge decision, H.R. 3621 appears to represent a precipitous action that is both inappropriate and dangerous. Its passage would reverse a lot of hard work done by both Congressional staffs over the past six years; could disrupt the AT&T divestiture process; and would be unsettling to both the telecommunications industry and the investment community.

The FCC access charge decision of December 1982 represents a balanced approach to a complicated problem. In particular:

1. The reassignment of non-traffic-sensitive costs to the local rate payer is both economically sound and necessary in an increasingly competitive environment;

2. The phased-in approach is designed to avoid sudden dislocations in user rates, yet to be fully implemented by a time that local network bypass could become a serious problem to the local telephone companies; and

3. The absolute dollar increases in fixed telephone charges are hardly excessive when compared with recent increases in other utility rates or when considered in light of the historically declining real costs of telephone service.

As Congress knows full well, the restructuring of any industry is a complicated process. The introduction of competition and deregulation into the telecommunications industry has already produced a wealth of new products and services. The process, which Congress has been studying and supporting, is working, but cannot be accomplished without some tradeoffs.

The actions taken by the FCC, in their access charge decision, reflect these tradeoffs and are guided by the extremely tight time schedule imposed by the AT&T divestiture. I would fully expect the FCC decisions to be fine tuned in the future to reflect changing market conditions and policy objectives set forth by Congress. At this point in time, however, I would suggest that Congress accept the FCC access charge decision as a balanced approach to a needed industry pricing reform, and to forbear from imposing a hastily conceived solution of its own.

Sincerely,

WINSTON E. HIMSWORTH,
First Vice President.

PARALYZED VETERANS OF AMERICA,
Washington, D.C. July 28, 1983.

Hon. **HAROLD GREENE,**
U.S. District Court for the District of Columbia,
Washington, D.C.

DEAR JUDGE GREENE: On behalf of the members of Paralyzed Veterans of America, I respectfully request that you reserve judgment on the proposed transfer of embedded equipment for disabled individuals until AT&T more clearly and fully explains its intentions regarding this equipment. The importance of the availability of specialized equipment at reasonable, affordable prices is of great concern to disabled citizens.

On July 15, 1983, AT&T announced its plans to create an unregulated "National Special Needs Center" to serve disabled users and to require the Bell operating companies to transfer installed terminal equipment and inventories to this body. This could potentially lead to unregulated price increases for disabled individuals. It was the intent of Congress when it passed the "Telecommunications for the Disabled Act," Public Law 97-410, that disabled citizens have access to necessary telecommunications equipment at reasonable costs. It is the intent of P.L. 97-410 that local companies continue to offer equipment to disabled individuals on a subsidized basis.

For many disabled people telecommunications equipment serves as a vital link to our larger society. Specialized devices allow severely disabled individuals the opportunity to be more self-sufficient and self-supporting, and in certain instances, are the necessary link to vital emergency and medical care. Without subsidized equipment, many disabled individuals may lose access to essential telephone services.

Again, on behalf of the members of Paralyzed Veterans of America and all disabled citizens who rely upon specialized telecommunications equipment, I request that you reserve judgment regarding the proposed transfer. I understand that AT&T has agreed to meet with disabled individuals and their representatives during the week of August 1 and, hopefully, the results of this meeting will be included in your considerations.

Sincerely yours,

DOUGLAS K. VOLLMER,
National Legislative Director.

National Association of the Deaf,
Silver Spring, Md., July 28, 1983.

Hon. **Harold Greene,**
U.S. District Court for the District of Columbia,
Washington, D.C.

Dear Judge Greene: We are aware that Mr. Scott Rafferty filed a letter with you on July 22, 1983, discussing the disposition of embedded special equipment for disabled persons under the AT&T Consent Decree. Specialized terminal equipment is essential to permit disabled persons to communicate. This was recently acknowledged by Congress in the Telecommunications for the Disabled Act of 1982, P.L. 97-410.

The National Association of the Deaf is the largest consumer organization of deaf and hearing-impaired people in the United States. I am also writing on behalf of two other organizations which are actively involved in issues of deafness and necessary services: Telecommunications for the Deaf, Inc. and the American Deafness and Rehabilitation Association.

Special equipment is an integral part of the regulated service provided to disabled persons by their local telephone companies. We are concerned that the transfer of specialized equipment pursuant to the Consent Decree will create an unworkable situation. In comments filed by AT&T in FCC Docket CC83-427, AT&T indicates for the first time its plans to de-tariff this equipment.

AT&T has agreed to discuss this issue with representatives of the disabled community and to explain its intentions in a meeting tentatively scheduled for next week. We will report to you on the results of this meeting. We therefore respectfully request that the Court reserve judgment on the transfer of specialized equipment in any order to approve the plan of re-organization.

Sincerely,

Albert T. Pimentel,
Executive Director.

[Mailgram]

New Jersey Coalition of Citizens Disabilities,
Midland Park, N.J., July 24, 1983.

U.S. **Senate Subcommittee on Telecommunications,**
Senate Office Building,
Washington, D.C.

Gentlemen: We are disturbed to hear that the possiblites for access to phone directories, operator informational services, and special adaptive equipment might be curtailed or greatly increased in cost to the blind, visually impaired and print handicapped disabled communities as a result of the recent judicial settlements revolving about the AT&T divestiture case.

The alleged proposal by the new local service companies for a new charge for printed directories along with a proposed national standard of charging for all informational calls places a bling, visually impaired or print handicapped individual in the impossible situation of either not being able to afford the local directory, nearby geographical phone directories, or leaving the necessity of costly charges for operator information calls.

The deterioration of the operator informational service by local companies is also a problem, strict time study standard for information operators have led to short, unintelligible and sometimes demeaning answers to questions about phone numbers for persons with long names. The new policy of not giving street addresses of public agencies or services is also unacceptable.

Many of the proposals seem designed to encourage this discontinuation of private and public telephone services to individuals below the poverty line, the majority of disabled individuals who are blind, visually impaired, print handicapped or who have speech difficulties fall below the poverty level according to the 1980 census data. The individual of moderate or middle income is also affected by increase cost and decreased acceptability to telephone services.

We are given to understand that many employees of the former Bell Systems including such groups as "The Pioneers", the CWA Union, lower income consumer groups, and groups of disabled individuals are requesting your oversight committee to investigate these proposed changes.

We hope that you will be able to assure the blind, visually handicapped and print handicapped communities that we will have access to affordable and necessary information service.

We also uge that the new local operating telephone companies not be permitted to avoid State public utility open public hearing about these subjects.

Due to late notice, we were unable to provide 50 copies of this mailgram by Monday July 25, but we request that it be read into the public record and transcript of your committee hearings.

Col. David Mayerowitz,
Middlesex County Commission on the Blind,
New Brunswick, N.J.

Steve Janick,
Midland Park, N.J.

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